PETITION FOR WRIT OF CERTIORARI

Supreme Court, U.S.
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No. 08-369

In The

Supreme Court of the United States

TRI-STATE FINANCIAL, LLC,

Petitioner,

v.

JOHN S. LOVALD, TRUSTEE OF THE CHAPTER 7 ESTATE OF TRI-STATE ETHANOL CO., LLC, *et al.*,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

I. Whether on a motion for recusal under 28 U.S.C. § 455, the judge-made timeliness doctrine may be invoked to bar discovery, a hearing, and opportunity to make a full record; to bar consideration of the circumstances establishing the substantive grounds for recusal under § 455(a) or § 455(b)(1); and, to bar consideration of the inapplicability of waiver under § 455(e).

II. Whether the judge-made doctrine of timeliness has given rise to unsettled questions, conflicts, and disarray — both inter-circuit and intra-circuit — relating to the doctrine's existence, application, and importance, thereby putting at risk the public's confidence in the integrity of the federal courts, undermining the independence of the judicial branch, and calling for an exercise by this Honorable Court of its supervisory power.

LIST OF PARTIES

Petitioner in this Court, plaintiff-appellant below, is Tri-State Financial, LLC.

Respondent in this Court, defendant-appellee below, is John S. Lovald, Trustee of the Chapter 7 Estate of Tri-State Ethanol Company, L.L.C.

Additional Respondents in this Court, defendants-appellees below, whose judgments are sought to be reviewed, are William F. Murphy Self Declaration of Trust; Michael D. Murphy; and Robert E. Hayes, of Davenport, Evans, Hurwitz & Smith.

RULE 29.6 STATEMENT

Pursuant to SUPREME COURT RULE 29.6, Petitioner states that it has no parent companies or non-wholly owned subsidiaries.

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PETITION FOR WRIT OF CERTIORARI

Petitioner Tri-State Financial, LLC ("TSF"), a creditor and party in interest in the Chapter 7 bankruptcy estate of Tri-State Ethanol Company, LLC ("TSE"), and also a holder of approximately 40% of the outstanding equity in TSE, respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eighth Circuit.

OPINIONS BELOW

The opinion of the Court of Appeals (App.[1] 1) is reported at *Tri-State Financial, LLC v. Lovald,* 525 F.3d 649 (8th Cir. 2008). The opinion of the district court (App. 15) is reported at *In re Appeals from Orders of the Bankruptcy Court in the Case of Tri-State Ethanol Co., LLC,* 369 B.R. 481 (D.S.D. 2007). The original opinion of the bankruptcy court (App. 66) is unreported.

JURISDICTION

The Judgment of the United States Court of Appeals for the Eighth Circuit sought to be reviewed was entered on May 13, 2008. Petitioner filed a timely petition for rehearing *en banc* which was denied on June 24, 2008. This Petition is timely

[1] "App." refers to the appendix attached hereto.

under SUPREME COURT RULE 13.1 as filed within 90 days of the date of denial of rehearing. This Court has jurisdiction to review the judgment of the Court of Appeals for the Eighth Circuit pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Due Process Clause of the Fifth Amendment to the United States Constitution provides in relevant part: "nor shall any person . . . be deprived of life, liberty, or property, without due process of law . . . " (App. 197).

The relevant provisions of 28 U.S.C. § 455 are reproduced at App. 197.

STATEMENT

The issue central to this Petition is whether the Court of Appeals for the Eighth Circuit ("Eighth Circuit") wrongly looked to its own judge-made "timeliness doctrine" as a stand-alone rule of first resort and controlling importance, dispositive of TSF's Motion for Recusal. One aspect of that issue is whether, in the interest of upholding Congress' purpose in enacting § 455, the timeliness doctrine is supported by concepts of waiver or forfeiture; a second aspect is whether a breach of judicial ethics

impacts upon § 455(a); and a final aspect is whether a § 455 movant is entitled constitutionally or otherwise to discovery, a meaningful hearing, and right to make a record. Also implicated is whether this Court should provide uniform rules for dealing with the foregoing issues as to rights to discovery, hearing, and making a full record; and also whether this Court should exercise its supervisory power to instruct the Eighth Circuit and other federal courts regarding any element of timeliness in the application of § 455 in order to foster the right of every federal litigant to a fair trial before a fair tribunal.

The Eighth Circuit, solely on the basis of its amorphous judge-made rule of timeliness, refused to consider the merits of TSF's motion for recusal of the bankruptcy judge ("Recusal Motion") in the bankruptcy case of TSE. The Eighth Circuit stated:

> Motions for recusal under 28 U.S.C. § 455 "*will not be considered* unless timely made." *Fletcher v. Conoco Pipe Line Co.*, 323 F.3d 661, 664 (8th Cir. 2003). The timeliness doctrine under § 455 "requires a party to raise a claim at the earliest possible moment after obtaining knowledge of the facts demonstrating the basis for such a claim." *Id.* . . .
>
> TSF's motion is untimely and, *on this basis alone*, the district court's decision to affirm the bankruptcy court's denial of the recusal motion is affirmed.

(App. 5-7) (emphasis added).

The Eighth Circuit's decision was based solely on the purported untimeliness of TSF's Recusal Motion, rendering the Eighth Circuit's "timeliness doctrine" a *per se* rule of law, absolutely barring any consideration of the merits of TSF's Recusal Motion. The merits which were not discussed and forever foreclosed from review, include the following grounds for recusal:

> (a) Whether it was an abuse of discretion or a denial of TSF's due process rights for the bankruptcy judge to deny TSF discovery, a hearing, and an opportunity to make a full record;
>
> (b) Whether the bankruptcy judge should have been disqualified prospectively from presiding over contested matters[2] and adversary proceedings[3] in which TSF was a party or held an interest because of any or all of the following:
>
> (i) His impartiality might be reasonably questioned under § 455(a) based on the accumulation of all of the circumstances;
>
> (ii) His actual bias against TSF, its members, and counsel under § 455(b)(1);
>
> (iii) His violations of Cannons 1, 2A, 3A(4) and (6), and 3C(1)(a) of the CODE

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[2] "Contested Matters" is defined in FED.R.BANKR.P. 9014.

[3] "Adversary Proceedings" is defined in FED.R.BANKR.P. 7001.

> OF CONDUCT FOR UNITED STATES JUDGES (including prohibitions against making public comments on the merits of a pending action, making *ex parte* communications, and failing to at all times act in a manner that promotes public confidence in the integrity and impartiality of the judiciary).

A. Due Process; 28 U.S.C. § 455

In 1955, this Court interpreted the Due Process Clause to provide to litigants the constitutional right to trial before judges that were free from bias and the appearance of bias:

> A fair trial in a fair tribunal is a basic requirement of due process. Fairness of course requires an absence of actual bias in the trial of cases. But our system of law has always endeavored to prevent even the probability of unfairness. . . . Such a stringent rule may sometimes bar trial by judges who have no actual bias and who would do their very best to weigh the scales of justice equally between contending parties. But to perform its high function in the best way justice must satisfy the appearance of justice.

In re Murchison, 349 U.S. 133, 136 (1955) (internal citation omitted).

In 1974, Congress made major revisions to 28 U.S.C. § 455, generally following the lead of the American Bar Association Model Code of Judicial Conduct. It clarified and broadened the grounds for

recusal in § 455(a) to include a new "catchall" requirement in § 455(a) that judges recuse themselves whenever their impartiality might reasonably be questioned. *Liteky v. U.S.*, 510 U.S. 540, 548 (1994). It changed the subjective "in the opinion of the judge" standard for evaluating grounds for recusal and required grounds for recusal to be evaluated on an objective basis. *Liljeberg v. Health Services Acquisition Corp.*, 486 U.S. 847, 857 (1988) ("*Liljeberg*").

In these major amendments, Congress provided no timeliness requirement; indeed, it rejected a recommendation from the Department of Justice that it do so. *See* H.R. REP. No. 1453, 93d Cong., 2d Sess. 9 (1974), *reprinted in* 1974 U.S.C.C.A.N. 6358. *See SCA Services, Inc. v. Morgan*, 557 F.2d 110, 117 (7th Cir. 1977) ("*SCA*").[4] Not withstanding this legislative history, most — if not all — circuits now read some judge-made timeliness rule into § 455(a), although the boundaries are uncertain, vary from circuit to circuit, and sometimes vary from case to case within a given circuit.

It is significant that the recusal issues here arise in a bankruptcy "case" created under 11 U.S.C. § 301. A "case" may include numerous "contested matters" and "adversary proceedings," FED.R.BANKR.P. 9014 and 7001, as does the TSE case.

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[4] An overlapping recusal statute, 28 U.S.C. § 144, does contain a timeliness requirement, but has no language comparable to § 455(a).

The recusal of bankruptcy judges is governed by 28 U.S.C. § 455. *See* § 455(f) (App. 200). Federal Bankruptcy Rule 5004(a) likewise recognizes that a bankruptcy case is not a single judicial unit and provides that a bankruptcy judge may be disqualified from presiding over the "proceeding," "contested matter," or "the case," as appropriate. As such, bankruptcy cases are unique in nature:

> Unlike the typical civil action, a bankruptcy proceeding is an "umbrella" under which a number of distinct, varied controversies are resolved. . . . Bankruptcy Rule 5004 also acknowledges the unique nature of bankruptcy proceedings. . . .

In re Apex Oil Co., 981 F.2d 302, 304 (8th Cir. 1992).

B. Background

TSE was created to build, own, and operate an ethanol plant in South Dakota. When TSE's ethanol plant was completed, it failed to work. As a consequence, in May 2003, TSE filed a voluntary Chapter 11 case in bankruptcy court in South Dakota. The South Dakota bankruptcy court acquired jurisdiction over TSE's bankruptcy case under 28 U.S.C. § 1334. No plan was confirmed; TSE's Chapter 11 case was eventually converted to Chapter 7.

TSF was created after the Chapter 11 filing to provide funding to TSE to facilitate retrofitting of the unproductive ethanol plant. As noted previously, TSF holds approximately 40% of the outstanding equity in

TSE. For providing funding in TSE's Chapter 11 case, TSF holds an unpaid allowed unsecured claim in the amount of $1.19 million, subordinated to other allowed unsecured claims.

TSE's Chapter 7 trustee ("trustee") initially disputed whether the assets of the Chapter 7 case were sufficient to pay TSF's claim in full. However, there now appears to be sufficient funds in the Chapter 7 estate to pay such claim in full, plus a return for some — if not all — equity holders.

The bankruptcy judge holds an unyielding predisposition to rule against TSF and its members because TSF funded the retrofitting of TSE's ethanol plant. The judge had denied a motion by TSE for authorization to enter into a contract to retrofit the plant. In its motion, TSE had requested the retrofitting be financed by a package of superpriority loans, secured by priming liens on all TSE's property. TSE and TSF, on advice of former counsel, believed that retrofitting, without the requested financing package, did not violate the Bankruptcy Code or the bankruptcy judge's order denying superpriority financing; they further believed that no order had to be obtained for making the plant operable, facilitated by unsecured loans that were at risk of not being paid. TSE went ahead with the retrofitting mostly on credit from its retrofitting contractor; TSF supplied partial financing without the benefit and protecton of secured loans.

TSF advised its members that the loans were at risk of not being repaid from the bankruptcy estate, and TSE put the same notice of risk in its Disclosure Statement, which was approved by the bankruptcy court. This risk was taken based on the business judgment that retrofitting the plant back to operational status was crucial to avoid Chapter 7 liquidation, where creditors would be paid pennies on the dollar and equity holders would recover nothing.

TSE's and TSF's business judgment proved correct: the retrofitting more than doubled the value of the ethanol plant. It enabled both secured creditors who would not have been paid in full and unsecured creditors who may not have been paid at all to be paid in full. No proceeding was ever brought against TSE or TSF for unauthorized retrofitting or financing of the plant.

Nonetheless, the bankruptcy judge was, and still is, convinced that TSE disobeyed his order denying TSE's motion for retrofitting with the superpriority, priming lien package. That perception festered; and the judge's pattern of bias began to unfold at a July 28, 2004, confirmation hearing. At that hearing (although TSE withdrew its request for confirmation), the bankruptcy judge stated on the record his view that TSE and TSF had abused the bankruptcy system, attempted to squeeze out equity holders other than TSF, and had participated in the filing of the bankruptcy case in bad faith.

Beginning with his July 29, 2004, order converting TSE's Chapter 11 case to Chapter 7, the bankruptcy judge started making rulings adverse to TSF. At first, these orders plausibly could be interpreted as rulings on the merits based on the application of bankruptcy law. However, as time passed, it became more and more apparent that the bankruptcy judge was intent on not allowing TSF or its members to prevail on any substantial dispute. As the rulings continued, it became more and more clear that TSF was not consistently pressing the wrong legal arguments and that the adverse rulings had to be explained in some other way. At a May 4, 2006, hearing the bankruptcy judge made comments that in substance revealed that he continued to harbor the belief that TSF had abused the bankruptcy process, attempted to squeeze out other equity, and participated in bad faith in the filing of the Chapter 11 petition. He also stated he had in mind a dollar limit that TSF should recover on its claim, so long as it was mostly subordinated to other claims; he indicated he was going to rule on TSF's claim and on other disputed claims in such a way that would limit TSF's recovery; and he stated that, although retiring, he was going to "keep this case" and go on recall status "to finish this case." Prior to the May 4 hearing, he had expressed the view that TSF had breached settlement agreements with the general contractor who had built the

plant (although no evidentiary hearing had been held on these issues).[5]

TSF has actively attempted to protect its prospects of recovery by opposing disputed claims in TSE's Chapter 7 case (which TSF contends the trustee should have opposed — but did not). Obviously, any gain from successful objections flows down to TSF's subordinated claim and to equity holders. As a result, in the ongoing Chapter 7 case, TSF is a litigant in contested matters and adversary proceedings and will be a litigant in future contested matters and adversary proceedings. Amounts disputed in the contested matters and in the adversary proceedings are over $10 million.

The effect of the Eighth Circuit's decision is not merely that TSF did not prevail in the particular contested matters appealed, involving approximately $800,000. The effect is also that TSF has been forced to litigate past, pending, and future contested matters and adversary proceedings involving over $10 million before an actually or apparently biased judge.

C. The Recusal Motion

On June 29, 2006, TSF filed its Recusal Motion, seeking to recuse the bankruptcy judge in contested

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[5] Unlike judicial rulings which in and of themselves "almost never constitute a valid basis" for a recusal motion, "surrounding comments or accompanying opinion" may. *Liteky v. U.S.*, 510 U.S. 540, 555 (1994).

matters and adversary proceedings in which TSF was a party or had an interest. TSF brought the Recusal Motion under § 455(a) (appearance of lack of impartiality), § 455(b) (actual bias), case law (violations of judicial code of conduct), and the Fifth Amendment (violation of procedural due process).

The accumulation of circumstances upon which TSF based its Recusal Motion were that the bankruptcy judge:

> (1) held a private conference with a newspaper reporter wherein he discussed the merits of TSE's pending bankruptcy case and, contrary to judicial ethics, expressed hostility and animus toward TSF, its members, and attorney;[6]
>
> (2) did not disclose to TSF's counsel his hostility toward a member of and key witness for TSF whom he believed had "hit on" the bankruptcy judge's law clerk;
>
> (3) had manifested bias, or at least the appearance of bias, towards TSF through a pattern of rulings and course of conduct, including comments;

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[6] The newspaper reporter signed her affidavit on June 12, 2006, in Roshalt, South Dakota, and mailed it to Omaha, Nebraska. The affidavit was attached to the Recusal Motion, filed from Omaha on June 29, 2006.

(4) made pejorative and denigrating comments about TSF, its members, and its attorney, accusing TSF of abusing the bankruptcy process, participating in TSE's purported bad faith Chapter 11 filing, and allegedly breaching settlement agreements;

(5) issued "status letters" in disputes over TSF's claim and in other proceedings which gave roadmaps to TSF's adversaries and otherwise prejudiced TSF;

(6) gave less favored treatment to TSF than its adversaries and did not allow TSF sufficient time to prepare for hearings;

(7) indirectly forced settlements which improperly subordinated TSF's claim and all claims of others associated with retrofitting TSE's ethanol plant — even though the retrofitting more than doubled the value of the plant and enabled creditors who probably would have received nothing to be paid in full;

(8) disallowed claims of members of TSF on grounds not applied to claims of any other creditors; and

(9) allowed administrative expenses and secured and unsecured claims of other creditors in excessive amounts, minimizing TSF's recovery, if not on its subordinated $1.19 million claim, on its 40% equity interest.

D. Denial of Discovery, Hearing, Complete Record

The bankruptcy judge denied TSF's timely requests for discovery (deposition of trustee) and a hearing on TSF's Recusal Motion. TSF had no opportunity to develop a full record to support the Recusal Motion. Instead, the bankruptcy judge conducted a straw poll of the attorneys representing other litigants in the Chapter 7 case, requesting their views concerning the Recusal Motion. *See* RESOLUTION G, PROCEEDINGS OF THE JUDICIAL CONFERENCE OF THE UNITED STATES (1971 Conf. Rept., pp. 68-69) ("a federal judge should reach his own determination as to whether he should recuse himself . . . without calling upon counsel to express their views as to the desirability of his remaining in the case"). *See also Southwestern Bell Telephone Co. v. F.C.C.*, 153 F.3d 520, 521 n.1 (8th Cir. 1998) (adhering to RESOLUTION G).

E. Recusal Denial

On the day of the deadline for responding to the straw poll, the trustee filed a response attaching an affidavit consisting of 8 pages and 38 paragraphs. On September 1, 2006, the bankruptcy judge issued a 117-page opinion and an order denying TSF's Recusal Motion (collectively, "Recusal Denial") (App. 66). In his opinion, the bankruptcy judge *sua sponte* attempted to create a selective record of events, covering the more than two years TSE's bankruptcy case

was pending (App. 151); on that record, he found that recusal was not justified. He quoted at length the Chapter 7 trustee's affidavit. (*See, e.g.*, App. 117-123; 147-149; 175). TSF was given no opportunity to participate in making a record nor to object to the record created by the bankruptcy judge.

F. Appeals

Because an order denying recusal is interlocutory and cannot be appealed as a matter or right, *Liddell v. Board of Ed. of City of St. Louis*, 677 F.2d 626, 643 (8th Cir. 1982), *cert. denied*, 459 U.S. 877 (1982), TSF appealed the Recusal Denial in conjunction with its appeals in two separate contested matters involving Robert E. Hayes of Davenport, Evan, Hurwitz & Smith; the William F. Murphy Self Declaration of Trust; and Michael D. Murphy (collectively "Appealed Contested Matters"). The bankruptcy judge, after denying recusal, entered final, appealable orders adverse to TSF in the Appealed Contested Matters.[7]

TSF appealed the Recusal Denial and orders entered in the Appealed Contested Matters to the district court; the district court affirmed. TSF then appealed to the Eighth Circuit; the Eighth Circuit affirmed.

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[7] In the Appealed Contested Matters, the Eighth Circuit affirmed both the bankruptcy court's judgments and the district court's affirmances.

G. Eighth Circuit Ruling

The Eighth Circuit refused to consider the merits of TSF's Recusal Motion on the grounds that "motions for recusal under 28 U.S.C. § 455 will not be considered unless timely made" (App. 5) (internal citation omitted). The Eighth Circuit did not consider whether TSF was entitled to discovery, a hearing, or a full and accurate record; it did not consider whether any of the grounds for recusal existed under § 455(a) or (b) or the Fifth Amendment, or breach of judicial ethics; and it did not consider whether or not the Recusal Motion was filed for tactical or strategic reasons. On grounds of what it considered untimeliness alone, it affirmed the Recusal Denial and denied TSF's timely filed petition for rehearing (App. 5-7). In determining timeliness, the circuit failed to consider that TSF was required, under circuit law, to presume the bankruptcy judge's impartiality; as such, TSF was required to allow the pattern of disqualifying events to unfold over time, to the point of establishing bias, before filing its Recusal Motion.

REASONS FOR GRANTING THE PETITION

As Congress recognized when it amended § 455(a) in 1974, recusal of federal judges that appear to be or are biased is inseparable from public confidence in the integrity of the federal judiciary. *Liljeberg*, 486 U.S. at 865 ("The very purpose of § 455(a) is to promote confidence in the judiciary by avoiding

even the appearance of impropriety when possible."). The concern over public confidence in the integrity of the federal judiciary has constitutional dimensions. *Id.* n.12 (citing *Aetna Life Ins. Co. v. Lavoie,* 475 U.S. 813 (1986)).[8]

The decision below, refusing to consider the Recusal Motion on its merits, pits a judge-made doctrine of timeliness against the federal law contained in § 455(a), (b)(1), and (e). The decision below conflicts with the decisions of this Court and other circuit courts of appeals, requiring recusal issues to be decided upon review of all of the circumstances of record and identification of those facts which place a judge's impartiality in question. The decision below also conflicts with § 455 decisions in other circuits that do not recognize a timeliness doctrine; that hold timeliness is only one of the factors to consider in determining recusal; that apply the timeliness doctrine to accumulated events by starting the clock only with the last in the sequence; and that reject a *per se* rule of timeliness which bars review on the merits.[9]

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[8] Legislative history of § 455(a) indicates that § 455 is "as much a protection for the citizenry as for the complaining [party]." *U.S. v. Brinkworth,* 68 F.3d 633, 637 (2d Cir. 1995).

[9] Although the decision below directly conflicts with decisions in other circuits, as shown below, decisions within a particular circuit, including the Eighth Circuit, often conflict with each other and put the law of the particular circuit in question. This points to disarray and confusion on § 455 issues both inter- and intra-circuit, all of which calls for an exercise of this Court's supervisory powers.

The decision below also raises recurring and important questions as to whether § 455 rights can ever be waived or forfeited under the timeliness doctrine; whether a judge's serious breach of judicial ethics is a factor that may override timeliness considerations; and whether the denial of discovery, the opportunity for a meaningful hearing at a meaningful time, or the opportunity to make a full, accurate record, or any of them, violate procedural due process — or are at least an abuse of discretion.

I. THE TEACHING OF THIS COURT, WHICH THE SECOND CIRCUIT ANTICIPATED AND THE FIFTH CIRCUIT ACKNOWLEDGES, IS THAT § 455(a) AND (b)(1) DISPOSITIONS MUST BE MADE UPON REVIEW OF ALL OF THE CIRCUMSTANCES AND IDENTIFICATION OF ALL OF THE FACTS SUPPORTING RECUSAL.

As noted, the Eighth Circuit clearly did not consider the merits of TSF's Recusal Motion: "TSF's Motion is untimely and, on this basis alone, the district court's decision to affirm the bankruptcy court's denial of the recusal motion is affirmed" (App. 6-7). As such, the Eighth Circuit conflicts with § 455 decisions of this Court and decisions of the Second and Fifth Circuits.

A. *Sao Paulo* and *Liljeberg*. This Court, in *Sao Paulo State of Federative Republic of Brazil v. American Tobacco Co.*, 535 U.S. 229 (2002) ("*Sao Paulo*")

expressly instructs that the decision whether to grant a motion to recuse under § 455(a) requires consideration from the perspective of "a reasonable person, *knowing all the circumstances.*" *Id.* at 232 (internal quotation omitted) (emphasis in original). Citing *Liljeberg*, this Court held that the issue of whether a judge's impartiality might reasonably be questioned "should not . . . [be] made in disregard of . . . [relevant] facts . . . ". *Id.* at 233. In *Liljeberg,* this Court instructs that in considering a motion for recusal under § 455(a), "it is critically important . . . to identify the facts that might reasonably cause an objective observer to question [a judge's] . . . impartiality." 486 U.S. at 865.

The decision below conflicts with *Sao Paulo* and *Liljeberg,* which require the Eighth Circuit to affirm the Recusal Denial only if it determined that the district court had reviewed the factual record for "all the circumstances" which, if known, would cause an objective person to reasonably question the bankruptcy judge's impartiality. The Eighth Circuit chose not to do so and affirmed on the basis of its own view that TSF's Recusal Motion was not "timely made."[10]

A natural consequence of the Eighth Circuit's sole reliance on its timeliness rule is to encourage lower courts in the Eighth Circuit to disregard this

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[10] The Eighth Circuit did not explain the standard of review it applied to reach that conclusion, but appears to have made its decision as a matter of law.

Court's instructions in *Sao Paulo* and *Liljeberg*. This is an abdication of the Eighth Circuit's supervisory power over district and bankruptcy courts in the circuit.

B. Second and Fifth Circuits. The rule in the Second Circuit, apparently anticipating *Sao Paulo* and *Liljeberg*, is that "the actual time elapsed between the events giving rise to the charge of bias or prejudice and the making of the motion is not necessarily dispositive." *Apple v. Jewish Hosp. and Medical Center*, 829 F.2d 326, 333-34 (2d Cir. 1987). The appellate court's review under § 455(a) must be guided by a comprehensive and independent examination of the facts and circumstances of the litigation. *See id.* The rule of the Fifth Circuit, following *Sao Paulo*, is the same. *See Andrade v. Chojnacki*, 338 F.3d 448, 455 (5th Cir. 2003) ("Another maxim [for interpreting § 455(a)] is that review should entail a careful consideration of context, that is, the entire course of judicial proceedings, rather than incidents.") (citing *Sao Paulo*), *cert. denied*, 541 U.S. 935 (2004); *F.T.C. v. Namer*, 2007 WL 2974059 at *4 (5th Cir. 2007) (unpublished opinion).

II. THE DECISION BELOW CONFLICTS WITH SIXTH, SEVENTH, AND NINTH CIRCUIT DECISIONS THAT § 455 MOTIONS ARE NOT SUBJECT TO ANY TIMELINESS REQUIREMENT.

The Eighth Circuit's timeliness rule is more fully stated in *In re Kansas Public Employees Retirement System*, 85 F.3d 1353 (8th Cir. 1996) ("*KPERS*"):

> We have held in the past that even though § 455 has *no express timeliness requirements, claims under § 455 will not be considered unless timely made. Holloway v. U.S.*, 960 F.2d 1348 (8th Cir. 1992); *see Oglala Sioux Tribe v. Homestake Mining Co.*, 722 F.2d 1407, 1414 (8th Cir. 1983) ("Although § 455 does not include an explicit time limitation, we believe that a timeliness requirement is appropriate . . . ".); *United States v. Bauer*, 19 F.3d 409, 414 (8th Cir. 1994) ("This court has held that claims under § 455 'will not be considered unless timely made.'") (quoting *Holloway*).

85 F.3d at 1360 (emphasis added).[11] This timeliness requirement conflicts with decisions in the Seventh, Sixth, and Ninth Circuits.

A. Seventh Circuit. The Seventh Circuit was probably the first to eschew a timeliness requirement for § 455 motions (per the 1974 amendments) and did so expressly:

> As a defense to the proceedings . . . , respondent . . . claims that disqualification is not required because SCA has waived its right to enforce section 455. As evidence of

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[11] An Eighth Circuit panel has suggested there is no timeliness requirement for § 455(a) motions. *See U.S. v. Tucker*, 78 F.3d 1313, 1324 (8th Cir.) (holding that § 455(a) had no timeliness requirement), *cert. denied*, 519 U.S. 820 (1996). However, *KPERS* explicitly discredits that holding, 85 F.3d at 1360, as does the instant case, implicitly. *See* note 9, *supra*.

> its position [respondent] notes the numerous proceedings which have been had in this case since SCA learned of the existence of the familial relationship. . . .
>
> The provisions [of § 455] are mandatory; they are addressed to the judge and require that he disqualify himself in certain circumstances. They were adopted because the drafters of the statute believed that confidence in the impartiality of federal judges is enhanced by a more strict treatment of waiver. They impose no duty on the parties to seek disqualification nor do they contain any time limits within which disqualification must be sought. Moreover, although the Department of Justice recommended that the new section 455 should include some limitation of time to prevent applications for disqualification from being filed near the end of a trial when the underlying facts were known long before, . . . Congress did not incorporate this recommendation in the statute.

SCA, 557 F.2d at 117 (internal citation omitted). *See also U.S. v. Balistrieri*, 779 F.2d 1191, 1203 n.12 (7th Cir. 1985) ("it is currently the law of this circuit that there is no time limit on a motion for recusal under § 455"), *cert. denied*, 475 U.S. 1094 (1986). *SCA* has been questioned on several occasions. *See, e.g., In re National Union Fire Ins. Co. of Pittsburg, Pa.*, 839 F.2d 1226, 1232 (7th Cir. 1988) (questioning, but refusing to revisit, whether *SCA* should be reconsidered because other courts of appeals have reached

opposite conclusion); *U.S. v. Murphy,* 768 F.2d 1518, 1539 (7th Cir. 1985) (decision in *SCA* stands alone; several courts have held that Congress did not put time limit in § 455 because time limits were already firmly fixed in both statute and common law), *cert. denied*, 475 U.S. 1012 (1986); *Schurz Communications v. F.C.C.*, 982 F.2d 1057, 1060 (7th Cir. 1992) (*SCA* is weak precedent; however, arguable that requirement of a timely filing of a recusal motion is not firmly established in this circuit).[12]

B. Sixth Circuit. Although *Easley v. University of Michigan Bd. of Regents,* 853 F.2d 1351 (6th Cir. 1988) does not expressly hold there is no timeliness requirement for § 455 motions, it does state that § 455 is self-executing, implying that at least in the trial court there is no need for recusal motions at all:

> Nonetheless, the procedural shortcomings of *Easley's* motion do not bar our consideration of its merits under the separate disqualification provisions of § 455.
>
> Section 455(a) is a self-executing provision for the disqualification of federal judges. There is no particular procedure that a party must follow to obtain judicial disqualification under § 455(a). Instead, this section sets forth a mandatory guideline that federal judges must observe *sua sponte*.

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[12] See note 9, *supra*.

Id. at 1357. *Accord U.S. v. Beasley,* 2006 WL 3511146 at *2 (E.D. Tenn. 2006) (unpublished opinion). *Cf. U.S. v. Campbell,* 59 Fed.Appx. 50 at **1 (6th Cir. 2003) (unpublished opinion) (declining to consider recusal issues not raised in the district court).[13]

The holding that § 455 is self-executing requiring *sua sponte* recusal conflicts with the Eighth Circuit rule that recusal motions are not considered unless timely made.

C. Ninth Circuit. In *In re Manoa Finance Co.,* 781 F.2d 1370 (9th Cir. 1986), *cert. denied,* 479 U.S. 1064, *reh'g denied,* 480 U.S. 991 (1987), the court acknowledged that although § 455 is stated in terms of a self-enforcing obligation upon the judge, it may be invoked by a party; and there is no requirement to even raise recusal at trial:

> Though section 455 is stated in terms of a self-enforcing obligation upon the judge, it may be invoked by a party. . . . There is no indication in the record that [movant] raised this issue below, but his failure to move for recusal at the trial level does not preclude his raising the issue on appeal.

Id. at 1373 (internal citation omitted). *Cf. Palila v. Hawaii Dept. of Land & National Resources,* 852 F.2d 1106, 1110 n.7 (9th Cir. 1988) (citing *Manoa* and stating, "[u]nder . . . § 455, it is unsettled in this

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[13] See note 9, *supra.*

circuit whether a claim must be timely"). *But see Skokomish Indian Tribe v. U.S.*, 410 F.3d 506, 519 (9th Cir. 2005) (*en banc*) ("A motion for recusal must be made with reasonable promptness after the ground for such motion is ascertained.") (internal citation omitted), *cert. denied*, 546 U.S. 1090 (2006).[14]

III. THE DECISION BELOW CONFLICTS WITH DECISIONS IN THE THIRD AND FEDERAL CIRCUITS THAT TIMELINESS IS ONLY ONE FACTOR TO CONSIDER IN DECIDING RECUSAL MOTIONS.

The Eighth Circuit's elevation of its timeliness rule to a rule of primacy that resulted in its refusal to consider TSF's Recusal Motion on the merits is in direct conflict with the Third Circuit rule that timeliness is only one factor to consider in deciding whether recusal is appropriate. *See In re Kensington Int'l, Ltd.*, 368 F.3d 289, 312 (3d Cir. 2004) ("timeliness . . . is but one of the factors" in determining a recusal motion). It also conflicts with the ruling of the Federal Circuit in *Polaroid Corp. v. Eastman Kodak Co.*, 867 F.2d 1415, 1418 (Fed. Cir.) ("The passage of time is merely one factor and events preceding the motion require equal if not greater consideration."), *cert. denied*, 490 U.S. 1047 (1989).

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[14] See note 9, *supra*.

IV. THE DECISION BELOW CONFLICTS WITH THE DECISION OF THE FIRST CIRCUIT THAT IF AN ACCUMULATION OF EVENTS IS THE BASIS FOR RECUSAL, A MOTION IS TIMELY IF FILED PROMPTLY UPON THE LAST OF THE ACCUMLATED EVENTS.

In the instant case, the Eight Circuit's paramount timeliness doctrine virtually nullifies its own rule that a violation of § 455(a) may be established by a course and pattern of rulings and course of conduct. *Cf. Moran v. Clarke,* 296 F.3d 638, 649 (8th Cir. 2002) (*en banc*) (since the inquiry under § 455(a) includes "all the relevant facts," it "warrants consideration of the judge's pattern of rulings, and also . . . course of conduct").[15] It does this by requiring *sub silentio* that each time a potentially disqualifying incident occurs, a movant must file an individual motion for recusal. This construct defies the practical reality that, in cases such as this, it is the accumulation of incidents over time that establishes grounds for recusal.

The Eighth Circuit failed to recognize the nature of recusal under § 455 based upon an accumulation of incidents. An accumulation of incidents takes time to unfold as a pattern.

Conflicting with the decision below is the First Circuit's view that although disqualifying events may accumulate over time, a motion promptly filed upon

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[15] See note 9, *supra*.

the last event of the accumulation is timely. The First Circuit, in reviewing "an accumulation of events," stated: "[a] motion to recuse is a very serious matter and must have a factual foundation; it may take some time to build the foundation." *In re U.S.*, 441 F.3d 44, 65-68 (1st Cir.) (recusal motion based on an accumulation of events; movant did not waive claim by filing promptly after the relevance of those events became clear), *cert. denied*, 127 S.Ct. 288 (2006).

Litigants should not lose their right to recuse a judge because they treat recusal — especially in the context of an accumulation of events — as a "very serious matter." This is particularly true because litigants are required to presume that the judge is impartial. *See Fletcher v. Conoco Pipe Line Co.*, 323 F.3d 661, 664 (8th Cir. 2003) ("*Fletcher*") ("a judge is presumed to be impartial and the party seeking disqualification bears the substantial burden of proving otherwise").

V. THE DECISION BELOW CONFLICTS WITH THE DECISIONS OF THE FIFTH, NINTH, AND ELEVENTH CIRCUITS THAT THERE IS NO *PER SE* TIMELINESS RULE.

The Eighth Circuit's decision not to consider the merits of a § 455 motion solely on the basis that it was not timely made is a *per se* rule — or tantamount to such rule. It conflicts with decisions in other circuits holding that there is no *per se* rule of timeliness. At least three other circuits have so held. *See*

Andrade v. Chojnacki, 338 F.3d 448, 455 n.5 (5th Cir. 2003) (declining to adopt a "*per se* rule" of untimeliness); *E. & J. Gallo Winery v. Gallo Cattle Co.,* 967 F.2d 1280, 1295 (9th Cir. 1992) (stating there is no "*per se* rule" of timeliness); *Summers v. Singletary,* 119 F.3d 917, 921 (11th Cir. 1997) (noting other jurisdictions have declined to adopt a *per se* rule on timeliness, "and neither will we"), *cert. denied,* 523 U.S. 1005 (1998).

VI. THE DECISION BELOW RAISES IMPORTANT AND RECURRING ISSUES OF THE APPROPRIATENESS OF WAIVER AND FORFEITURE UNDER § 455(e).

In the decision below, the Eighth Circuit appears to treat its "timeliness doctrine" as being *sui generis,* sufficient in and of itself to bar TSF's claim on its merits. However, given other Eighth Circuit § 455 decisions and those from other circuits, it must be assumed that the Eighth Circuit's timeliness doctrine is subsumed in broader theories of waiver and forfeiture.

For example, in *Fletcher,* the Eighth Circuit, affirming an order denying recusal under § 455, explained that conscious choice results in waiver, whereas inadvertent action results in forfeiture. 323 F.3d at 664. Likewise, in *U.S. v. Mathison,* 157 F.3d 541 (8th Cir. 1998), *cert. denied,* 525 U.S. 1165 (1999), the court found that the movant "did not simply forfeit [his right to recusal under § 455] by mere

inadvertent inaction; he made a conscious choice not to raise the objection" and concluded that, in those circumstances, it was plain the movant had waived his rights. *Id.* at 545-46. The Eighth Circuit limits appellate review of denial of recusal on whether the movant is deemed to have waived or forfeited the right:

> On appeal, the distinction between waiver and forfeiture is an important one. If a party waives a recusal claim, then judicial review is precluded. . . . If, however, a party forfeits an error, and the error is plain and affects substantial rights, then the court of appeals has authority to order correction, but is not required to do so.

Fletcher, 323 F.3d at 664 (internal citation omitted).

Other circuits also consider timeliness in making § 455 decisions in varying contexts of waiver or forfeiture. The Second Circuit adds the concept of implied waiver in its analyses. *See U.S. v. Bayless*, 201 F.3d 116, 127 (2d Cir.) ("confusion [between waiver and forfeiture] arises because untimeliness in making a motion for recusal can sometimes constitute the basis for finding an implied waiver"), *cert. denied*, 529 U.S. 1061 (2000). In the Seventh Circuit, before a claim for recusal can be deemed forfeited, the claim

had to be "knowable" to the movant and not impeded by any cause. *U.S. v. Murphy*, 768 F.2d at 1540.[16]

Clearly, there is inconsistency among the circuits regarding how, if at all, theories of waiver and forfeiture intersect with timeliness considerations in § 455 motions. However, a paramount question is whether wavier (except to the extent expressly authorized under § 455) and forfeiture — or their equivalents, shrouded by timeliness rules — should apply to § 455 decisions. Congressional intent underlying § 455 and opinions from this Court compel the conclusion that they should not.

The statute permits waiver only in clearly delineated circumstances. Subsection (e) absolutely prohibits any waiver by a litigant of such litigant's right to trial before an actually biased judge: "No justice, judge, or magistrate judge shall accept . . . a waiver of any ground for disqualification enumerated in subsection (b)" (App. 200). Subsection (b)(1) requires recusal for actual bias (App. 198). Section 455(e) also prohibits acceptance of a waiver by a litigant of such litigant's right to recusal under § 455(a) for the appearance of questionable impartiality unless such waiver is "preceded by a full disclosure on the record of the basis for disqualification" (App. 200).

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[16] In the instant case, the pattern was not knowable until fully developed, was impeded by the judge's lack of § 455(e) disclosure, and further impeded in that single incidents were not sufficient individually for recusal, but became sufficient only after the pattern unfolded.

Nothing has been found in the legislative history of the 1974 revisions to § 455 that indicates Congress intended to incorporate into the statute any concept of waiver broader than that which is expressly stated; nothing has been found in such legislative history that indicates that Congress intended a theory of forfeiture, distinct from that of waiver, to apply. In fact, a contrary intent is implied from the legislative history: "Congress amended section 455 in 1974 to clarify and broaden the grounds for judicial disqualification and to conform with the recently adopted ABA Code of Judicial Conduct, Cannon 3C (1974)." *Fletcher*, 323 F.3d at 664 (quoting *Liljeberg,* 486 U.S. at 858 n.7). Clarifying and broadening the grounds for judicial disqualification does not reasonably suggest that Congress meant to expand waiver beyond the express words of the statute or *sub silentio* imply a theory of forfeiture.

Indeed, as this Court has instructed, forfeiture cannot be construed more broadly than the concept of waiver:

> Waiver . . . is merely one means by which a forfeiture may occur. Some rights may be forfeited by means short of waiver . . . but others may not. . . . A right that cannot be waived cannot be forfeited by other means (at least in the same proceeding) but the converse is not true.

Freytag v. C.I.R., 501 U.S. 868, 894 n.2 (1991) (Scalia, J., concurring) (internal citation omitted). Thus, for the Eighth Circuit and other circuits to hold that

§ 455 rights may be forfeited by means beyond the express provisions for waiver in § 455 is contrary to the terms of the statute, Congressional intent as reflected in legislative history, and the teachings of this Court as to the relationship between waiver and forfeiture.

In the decision below, the Eighth Circuit made no findings that would support the conclusion that TSF had either waived or forfeited its § 455 right to have its Recusal Motion heard on the merits. There was no finding that TSF had intentionally chosen not to timely raise its rights; there was no finding that TSF had somehow by its conduct inadvertently lost the right. The court erred in applying its "timeliness doctrine" *sui generis* so as to avoid a waiver analysis pursuant to statutory guidelines or to at least make findings that would support forfeiture under its own prior cases. The court further erred in applying its "timeliness doctrine" so as to avoid hearing TSF's Recusal Motion on the merits.

As such, the decision below raises the recurring and important question of whether, under the guise of a "timeliness doctrine," a litigant's recusal rights may ever be deemed waived under theories beyond what is expressly stated in § 455 or may ever be deemed forfeited, without any statutory authority for such. This Court should exercise its supervisory powers to

settle these questions which are vital for the uniform application of § 455.[17]

VII. THE DECISION BELOW RAISES IMPORTANT AND RECURRING QUESTIONS OF THE IMPACT OF VIOLATIONS OF JUDICIAL ETHICS ON § 455 MOTIONS.

The private interview that the bankruptcy judge gave to the newspaper reporter, wherein the judge commented extensively about the merits of TSE's pending Chapter 7 case and disparagingly commented about TSF, its members, and its attorney, violates Canons 1, 2A, 3A(4), 3A(6), and 3C(1)(a) of

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[17] TSF does not suggest that timeliness is never a consideration. Timeliness may be a factor when determining whether a recusal motion has been filed only for tactical and strategic reasons to manipulate results in the litigation. However, in this context, timeliness relates to whether a recusal motion is filed in bad faith — an issue that always may be addressed by a court under its inherent powers to regulate the integrity of its proceedings. *See Chambers v. NASCO, Inc.*, 501 U.S. 32, 46, 50-51 (finding federal courts have "inherent powers" to impose "appropriate" sanctions when, *inter alia*, "a party shows bad faith by delaying or disrupting the litigation . . . ") (internal citation omitted), *reh'g denied*, 501 U.S. 1269 (1991). *Accord Harlan v. Lewis*, 982 F.2d 1255, 1259 (8th Cir.) (citing *Chambers*), *cert. denied*, 510 U.S. 828 (1993). However, timeliness in this context is on a different footing than the use of timeliness to bar a good faith litigant's right to recuse a judge whose impartiality may be reasonably questioned. In the instant case, the trustee accused TSF of filing the Recusal Motion for tactical purposes; however, all evidence was to the contrary; and neither the bankruptcy court, the district court, nor the Eighth Circuit made any such finding.

the CODE OF CONDUCT FOR UNITED STATES JUDGES ("JUDICIAL CODE") (App. 202-04). The judge exacerbated the situation by not disclosing to TSF or its counsel the animus he held toward one of TSF's members because the judge believed the member had "hit on" the judge's law clerk. He further commented he did not mind seeing such member "sweat" when TSF initially lost the bid at the trustee's auction of the ethanol plant. By such conduct, the bankruptcy judge breached the foregoing provisions of the Judicial Code.

Canon 1 requires a judge to maintain and enforce high standards of conduct in order to "uphold the integrity and independence of the judiciary" (App. 202). Canon 2A requires a judge to "act at all times in a manner that promotes public confidence in the integrity and impartiality of the judiciary" (App. 202). Canon 3A(4) requires a judge to "accord to every [party] full right to be heard according to law" and requires a judge to "neither initiate nor consider *ex parte* comments on the merits, or procedures affecting the merits of a pending . . . proceeding" (App. 203). Canon 3A(6) requires a judge to "avoid public comment on the merits of a pending . . . action . . . " (App. 203-04). Canon 3C(1)(a), in essence, requires the judge to comply with § 455(a) (App. 204).

When the bankruptcy judge granted the interview by the newspaper reporter and proceeded to make *ex parte* comments on the merits of TSE's pending bankruptcy case and derogatory comments about TSE, its members, and its counsel, the judge

violated the foregoing Canons. Given this conduct, the judge violated not only Canon C(1)(a) but also § 455(a) by not *sua sponte* disqualifying himself. Although these violations apparently did not concern the Eighth Circuit, at least two other circuits have found violations of a similar nature so serious as to require disqualification. *See, e.g., In re Boston's Children First,* 244 F.3d 164 (1st Cir. 2001); *U.S. v. Microsoft Corp.,* 253 F.3d 34, 114 (D.C. Cir.), *cert. denied,* 534 U.S. 952 (2001); *U.S. v. Cooley,* 1 F.3d 985, 988 (10th Cir. 1993). In addition, the Fifth Circuit, in *Andrade v. Chojnacki,* citing the foregoing cases, held that charges that a judge violated the Judicial Code are serious charges, but did not review the charges because they had not been preserved for appeal. 338 F.3d at 459.

VIII. THE DECISION BELOW RAISES IMPORTANT AND RECURRING QUESTIONS REGARDING PROCEDURAL DUE PROCESS IN THE CONTEXT OF § 455 MOTIONS.

As noted, before issuing an order and 117-page opinion denying TSF's Recusal Motion (App. 65-194), the bankruptcy judge entered interlocutory orders that denied TSF the right to take the trustee's deposition about the contents of his affidavit, quoted extensively in the bankruptcy judge's opinion, and denied TSF the opportunity for hearing, argument, or to make a full record. The bankruptcy judge clearly substituted his 117-page opinion for the record:

> The court has attempted . . . to provide a sufficiently thorough review of what has transpired to date so it may appropriately consider the recusal motion filed by [TSF].

(App. 151).

This selective review was not a "record" at all; and, in any event, it was not a record in which TSF had any input, except to the extent of its Recusal Motion. Nor is the "review" a neutral and fair record. It contains inaccuracies, slanted versions of events and occurrences, omits material facts, and takes as true the trustee's argumentative affidavit.

It is axiomatic that "[t]he fundamental requirement of due process is the opportunity to be heard, at a meaningful time and in a meaningful manner." *Birdwell v. Hazelwood School Dist.*, 491 F.2d 490, 495 (8th Cir. 1974) (internal citation omitted). *Accord Satterfield v. Edenton-Chowan Bd. of Ed.*, 530 F.2d 567, 572 (4th Cir. 1975). Contrary to the Federal Rules of Civil Procedure, TSF was denied discovery. TSF was entitled to discovery under the circumstances of this case.[18] *See Cheeves v. Southern Clays, Inc.*, 797 F. Supp. 1570, 1580 (M.D. Ga. 1992) (discovery mechanisms of Federal Rules available to a party who in good faith wishes to establish relevant facts supporting recusal), *aff'd, without op.*, 39 F.3d 326 (11th Cir. 1994), *cert. denied*, 515 U.S. 1102 (1995).

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[18] TSF does not contend that a *per se* rule requires a hearing on every motion for recusal.

Consideration of whether "a reasonable person knowing all of the circumstances, would harbor doubts as to the judge's impartiality," implicates a right to discovery. *In re Kensington Int'l, Ltd.*, 353 F.3d at 223 (district judge presiding over a Chapter 11 case *sua sponte* stayed discovery on recusal motion; Third Circuit reversed, holding that record was incomplete and that stay prevented parties from developing adequate record on a § 455 motion). TSF likewise was entitled to a full record. *In re Federal Skywalk Cases,* 680 F.2d 1175, 1184 (8th Cir. 1982) ("A claim of bias must be evaluated in light of the full record, not simply in light of an isolated incident.").

Because TSF did not receive the procedural safeguards that due process requires — neither discovery, an opportunity to be heard at a meaningful time and in a meaningful manner, nor the opportunity to make a full record — TSF's Fifth Amendment rights of procedural due process were violated. *See Gordon v. Hansen,* 168 F.3d 1109, 1114 (8th Cir. 1999) ("To set forth a procedural due process violation, a plaintiff, first, must establish that his protected liberty or property interest is at stake. . . . Second the plaintiff must prove that defendant deprived him of such interest without due process of law") (internal citation omitted). These requirements have been met. As the court stated in *Shepherdson v. Nigro,* 5 F.Supp.2d 305 (E.D. Pa. 1998), "the right to a fair hearing and to an impartial decisionmaker are quintessential procedural rights. A denial of such rights is

thus generally viewed as implicating procedural due process." *Id.* at 308.

This Court has long recognized that procedural due process requires a right to a fair trial in a fair tribunal. In *In re Murchison,* this Court held that "[a] fair trial in a fair tribunal is a basic requirement of due process." 349 U.S. at 136. In *Ward v. Village of Monroeville, Ohio,* 409 U.S. 57 (1972), this Court stated that under due process of law a party "is entitled to a neutral and detached judge in the first instance." *Id.* at 60-62.

Had TSF been granted the opportunity to be heard in a meaningful way at a meaningful time, whether or not TSF's Recusal Motion was untimely would have been decided on the basis of evidence and arguments, instead of on the basis of conclusory statements in the record unilaterally created by the bankruptcy judge. Had TSF had an opportunity to be heard, the bankruptcy judge may have been convinced that he was duty bound to recuse himself; moreover, TSF would have at least been given the opportunity to make a complete record with testimony, available for review by the district court, the Eighth Circuit, and this Court.

CONCLUSION

TSF respectfully submits that for the foregoing reasons, and each of them, the errors of the Eighth Circuit may be rectified only by a reversal of the

Recusal Order, reversal of the judgments entered in the Appealed Contested Matters, reversal of all interlocutory and final orders entered by the bankruptcy judge, and remand of the same for new hearings before an impartial judge.

The Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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September 2008

United States Court of Appeals
FOR THE EIGHTH CIRCUIT

No. 07-2430

Tri-State Financial, LLC, *
*
Appellant, *
*
v. *
*
John S. Lovald; *
Murphy Brothers, *
*
Appellees. *

No. 07-2433

Appeals from the United States District Court for the District of South Dakota.

Tri-State Financial, LLC, *
*
Appellant, *
*
v. *
*
Robert E. Hayes; *
Davenport, Evans, *
Hurwitz & Smith, *
*
Appellees. *

Submitted: March 12, 2008
Filed: May 13, 2008

Before RILEY, GRUENDER, and SHEPHERD, Circuit Judges.

RILEY, Circuit Judge.

These consolidated cases arise out of the 2003 bankruptcy filing by Tri-State Ethanol Company, LLC (TSE), the owner of an ethanol plant near Rosholt, South Dakota. Tri-State Financial, LLC (TSF) purchased the ethanol plant from the bankruptcy estate and appeals, asserting the bankruptcy court[1] (1) abused its discretion in denying TSF's motion seeking the recusal of the bankruptcy judge; (2) erred in (a) approving a settlement negotiated by the bankruptcy trustee with an oversecured creditor contrary to TSF's objection, and (b) in denying TSF a hearing regarding the settlement approval; and (3) exceeded its authority and abused its discretion in allowing Robert E. Hayes (Hayes), an attorney retained by the bankruptcy trustee, to collect his fees in full despite a conflict of interest arising from Hayes's representation of both the trustee and an unsecured creditor.[2]

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[1] The Honorable Irvin N. Hoyt, Bankruptcy Judge for the United States Bankruptcy Court for the District of South Dakota.

[2] TSF also complains the bankruptcy court erred under Bankruptcy Rule 9019(a) when the court permitted the settlement creditor to participate as a party in the settlement approval proceeding, offering evidence and presenting argument. The bankruptcy court did not exceed its considerable equitable

(Continued on following page)

The district court[3] affirmed the decisions of the bankruptcy court. We affirm.

I. BACKGROUND

The William F. Murphy Self-Declaration of Trust and Mike D. Murphy (collectively, Murphy) loaned money to TSE to finance the construction of a pipeline to TSF's South Dakota ethanol plant. On May 23, 2003, TSE filed a Chapter 11 bankruptcy which was later converted to a Chapter 7 proceeding on July 29, 2004. On January 28, 2005, bankruptcy trustee John S. Lovald (Trustee) filed a motion in the bankruptcy court seeking authority to pay certain secured claims, including a partial payment to Murphy of $1,986,000 on Murphy's secured claim. On February 15, 2005, the bankruptcy court granted the Trustee authority to make the requested partial payment to Murphy on Murphy's secured claim. No unresolved objection to this payment was ever filed in the bankruptcy court.

On August 8, 2005, Murphy filed an amended proof of claim as an oversecured creditor in the amount of $2,526,324.75, plus post-petition interest and attorney fees. In August 2005, the Trustee negotiated a settlement with Murphy on Murphy's outstanding

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discretion, and finding no error, we conclude this complaint by TSF lacks merit.

[3] The Honorable Charles B. Kornmann, United States District Judge for the District of South Dakota.

claims for $675,886.80 and filed a motion to have the settlement approved on August 25, 2005.[4] The bankruptcy court held a telephonic status conference on October 12, 2005, involving representatives of TSF, the Trustee, and Murphy where the parties agreed that, in lieu of an evidentiary hearing scheduled for the next day, the parties would submit written arguments and agreed exhibits by November 14, 2005. The parties then had until November 29, 2005, to submit any responsive arguments. The parties accordingly submitted written briefs and responsive arguments. On January 22, 2007, this settlement was approved by the bankruptcy court over TSF's objections. The bankruptcy court found the settlement was a compromise which fell "within the range of reasonableness and [was] in the best interests of the estate."

TSF not only took exception to the Murphy settlement, but also took exception to many of the other actions of the bankruptcy court and also of the Trustee, eventually filing a motion on June 29, 2006, asking the bankruptcy judge to recuse himself. On September 1, 2006, the bankruptcy judge denied the motion in a thorough 117 page decision.

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[4] The Trustee discovered several accounting errors and other discrepancies in Murphy's claim. The settlement agreement estimated the benefits to the debtor's estate were approximately $800,000.

In August 2003, the Trustee retained Hayes to represent the Trustee in the TSE bankruptcy proceedings. Hayes also represented Clapper Corporation (Clapper), an unsecured creditor. Hayes disclosed this potential conflict, and both the Trustee and Clapper waived any conflict. The August 2003 attorney retention application disclosed to the court and creditors Hayes "is counsel for unsecured creditor Clapper Corporation." This appointment was approved without objection. Later, when Hayes sought payment for his services, TSF objected on the basis of a conflict in Hayes's representation of both the Trustee and Clapper. The bankruptcy court approved Hayes's fee request over TSF's objection.

TSF appealed to the district court the recusal motion denial; the Murphy settlement; and Hayes's fee approval. The district court affirmed the bankruptcy court's decisions. These appeals followed.

II. DISCUSSION

"As the second reviewing court, we apply the same standards of review that the district court applied . . . review[ing] the bankruptcy court's factual findings for clear error and its conclusions of law de novo." *In re Clark*, 223 F.3d 859, 862 (8th Cir. 2000).

A. Recusal

Motions for recusal under 28 U.S.C. § 455 "will not be considered unless timely made." *Fletcher v.*

Conoco Pipe Line Co., 323 F.3d 661, 664 (8th Cir. 2003) (citation omitted). The timeliness doctrine under § 455 "requires a party to raise a claim at the earliest possible moment after obtaining knowledge of facts demonstrating the basis for such a claim." *Id.* (internal quotation marks and citation omitted). A party is required to bring its recusal motion promptly to avoid the risk that the party might hold its application as an option in the event the trial court rules against it. *See In re Apex Oil Co.*, 981 F.2d 302, 304-05 (8th Cir. 1992).

TSF's motion was not timely. The issues TSF discusses as the bases for its motion were: (1) the December 12, 2003, denial of TSE's motion for multi-faceted relief; (2) the court's July 28, 2004, comments and ruling related to the conversion of the case to Chapter 7; (3) the court's actions at the October 26, 2004, auction of the ethanol plant and private comments the court made following the auction; and (4) a November 18, 2005, hearing where TSF's counsel intimated the court was being unfair. While these events occurred as early as December 2003 and then in 2004 and 2005, TSF did not make its recusal motion until June 29, 2006. The actions and comments TSF asserts for its recusal motion first occurred thirty months before the motion and last occurred seven months before the motion. Even measuring from the most recent event, a relatively lengthy seven months elapsed. TSF's motion is untimely and, on this basis alone, the district court's decision to affirm the bankruptcy court's denial of the

recusal motion is affirmed. *See In re Kansas Pub. Employees Retirement Sys.*, 85 F.3d 1353, 1360-61 (8th Cir. 1996) (finding a ten-month delay from the initial awareness of a potential conflict rendered the motion untimely).

B. Murphy Settlement Approval

"A bankruptcy court's approval of a settlement will not be set aside unless there is plain error or abuse of discretion." *In re Martin*, 212 B.R. 316, 319 (B.A.P. 8th Cir. 1997) (citing *In re New Concept Housing, Inc.*, 951 F.2d 932, 939 (8th Cir. 1991)). "An abuse of discretion occurs if the court bases its ruling on an erroneous view of the law or on a clearly erroneous assessment of the evidence." *In re Racing Servs.*, 332 B.R. 581, 584 (B.A.P. 8th Cir. 2005) (citing *Cooter & Gell v. Hartmarx Corp.*, 496 U.S. 384, 405 (1990)). The standard for evaluation of a settlement "is whether the settlement is fair and equitable and in the best interests of the estate." *Martin*, 212 B.R. at 319 (internal quotation marks and citation omitted) (relying, in part, on *Protective Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson*, 390 U.S. 414, 424 (1968)). A settlement is not required to constitute "the best result obtainable." *Id.*

> Rather, the court need only . . . determine that the settlement does not fall below the lowest point in the range of reasonableness.
>
> . . .

> In assessing the reasonableness of a settlement, the factors to be considered can be summarized as follows:
>
> (A) the probability of success in the litigation;
>
> (B) the difficulties, if any to be encountered in the matter of collection;
>
> (C) the complexity of the litigation involved, a[n]d the expense, inconvenience and delay necessarily attending it; and
>
> (D) the paramount interest of the creditors and a proper deference to their reasonable views in the premises.

Id. (internal quotation marks and citations omitted). Both the bankruptcy court and the district court considered this four factor test and found the first three factors weighed in favor of the settlement because (1) Murphy had a good chance of success in litigation considering Murphy was entitled to be paid both principal and interest under the contractual terms of the notes; (2) Murphy is an oversecured creditor and therefore would not have any difficulty in collecting the monies owed; (3) the litigation necessary to dispute Murphy's claim would be complex and protracted, and Murphy would be entitled to recover attorney fees and expenses from the petition date of May 23, 2003, through the appellate process; and (4) even though 52 entities were given notice of the proposed settlement, TSF was the only entity filing an objection. The lower courts also found Murphy

made significant concessions in (1) waiving pre-and post-petition attorney fees available under § 506; and (2) settling its claim for $675,886.80 which is almost $115,000 less than the amount of principal, interest and late charges accrued as shown in Trustee's Revised Exhibit 4 of $790,000. Based on a review of the four factor test and the totality of the circumstances, neither the bankruptcy court, nor the district court, abused its discretion in approving the Murphy settlement.

The bankruptcy court also did not abuse its discretion in denying TSF a hearing regarding the Murphy settlement. Rule 9019 states, "[o]n motion by the trustee and after notice and a hearing, the court may approve a compromise or settlement." The term "after notice and a hearing,"

> (A) means after such notice as is appropriate in the particular circumstances, and such opportunity for a hearing as is appropriate in the particular circumstances; but (B) authorizes an act without an actual hearing if such notice is given properly and if – (i) such a hearing is not requested timely by a party in interest. . . .

11 U.S.C. § 102(1). Here, a hearing was scheduled and notice of the hearing was properly given to TSF. TSF then agreed with the other parties and the court, or did not object to the proposed procedure, to cancel the scheduled hearing and to instead present the issue to the bankruptcy judge on written arguments. TSF submitted its written argument opposing the

settlement and also submitted a written response to the opposing argument. As such, TSF was properly notified of the proposed settlement and had an opportunity to participate in a hearing which was scheduled specifically to address the Murphy settlement. TSF was "heard" when TSF submitted its written arguments and evidence and the bankruptcy court considered the submitted evidence and arguments. Where TSF agreed to the cancellation of the formal hearing and was given the opportunity to submit its arguments in writing, the court did not abuse its discretion when it did not hold a formal hearing regarding the Murphy settlement.

C. Hayes's Attorney Fees

"[A] decision regarding [the award of] attorney fees [is reviewed] for an abuse of discretion." *In re Clark,* 223 F.3d 859, 862 (8th Cir. 2000) (citation omitted). "The bankruptcy court has the broad power and discretion to award or deny attorney fees, and, indeed, a duty to examine them for reasonableness." *Id.* at 863 (citations omitted). An assessment of the reasonableness of the compensation sought "is always a question of fact for the court." *Id.* (citation omitted). TSF does not challenge the reasonableness of Hayes's hourly rate or that Hayes did the work claimed. Instead, TSF argues the fees should have been reduced (or not paid at all) because of the conflict arising from Hayes's representation of both the Trustee and Clapper, an unsecured creditor.

Under 11 U.S.C. § 327(c), an attorney is not disqualified from representing the Trustee solely because the attorney represents a creditor unless a creditor objects to the employment and an actual conflict of interest exists. On August 3, 2004, when the Trustee filed an application with the court seeking to employ Hayes, the application disclosed Hayes "is counsel for unsecured creditor Clapper." At this time there was no actual conflict.[5] Hayes's appointment was approved without objection. Only later, in 2006, when Hayes sought payment for his services, did TSF object on the ground of a conflict in Hayes's representation of both the Trustee and Clapper.

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[5] The Trustee and Clapper both formally waived any conflict. We acknowledge nonbinding authority exists indicating the limitations in § 327 cannot be waived. *See In re American Energy Trading, Inc.*, 291 B.R. 154, 158 (Bankr. W.D. Mo. 2003) ("The adverse interest and disinterested person limitations set forth in § 327 governing the employment of professionals cannot be excused by waiver.") (citing *In re Envirodyne Indus., Inc.*, 150 B.R. 1008 (Bankr. N.D. Ill. 1993)). Section 327(a) permits the trustee, with court approval, to employ attorneys "that do not hold or represent an interest adverse to the estate." Section 327(c) mandates, upon objection by another creditor or by the trustee, "the court shall disapprove such employment if there is an actual conflict of interest." The court in *American Energy Trading* found an actual conflict of interest. *Id.* at 156-57 ("[T]he actual conflict that has been represented to the Court at the hearing, provides ample support for this Court to revisit its previous ruling."). Here, no actual conflict of interest existed. Because no actual conflict of interest exists, it is unnecessary for us to determine the effectiveness of the waiver by the Trustee and Clapper.

At no time did Hayes represent the bankruptcy estate in connection with any claims by Clapper. The Trustee employed a different attorney to represent the estate in challenging any claim by Clapper. No financial harm was suffered by the bankruptcy estate or any other party from this alleged conflict. Where TSF only challenges the fee award on the basis of a conflict, effectively not contesting whether the work was done or whether the hourly rate charged was reasonable, the court did not abuse its discretion in awarding Hayes the fees sought.

III. CONCLUSION

For the foregoing reasons, we affirm the district court and the subject challenged decisions of the bankruptcy court.

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No: 07-2430

Tri-State Financial, LLC,

Appellant

v.

John S. Lovald; Murphy Brothers,

Appellees

No: 07-2433

Tri-State Financial, LLC,

Appellant

v.

Robert E. Hayes; Davenport,
Evans, Hurwitz & Smith,

Appellees

Appeal from U.S. District Court
for the District of South Dakota
(1:06-cv-01040-CBK)
(1:07-cv-01003-CBK)

JUDGMENT

This appeal from the United States District Court was submitted on the record of the district court, briefs of the parties and was argued by counsel.

After consideration, it is hereby ordered and adjudged that the judgment of the district court in this cause is affirmed in accordance with the opinion of this Court.

May 13, 2008

Order Entered in Accordance with Opinion:
Clerk, U.S. Court of Appeals, Eighth Circuit.

/s/ Michael E. Gans

UNITED STATES DISTRICT COURT
DISTRICT OF SOUTH DAKOTA
NORTHERN DIVISION

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IN THE MATTER OF APPEALS FROM ORDERS OF THE BANKRUPTCY COURT IN THE CASE OF TRI-STATE ETHANOL COMPANY, LLC,	*	CIV 06-1040, 06-1043, and 07-1003
	*	**2007 D.S.D. 9**
	*	ORDER AND OPINION
Debtor.	*	(Filed May 17, 2007)

****

KORNMANN, U.S. DISTRICT JUDGE

[¶1] The bankruptcy case of Tri-State Ethanol Company, LLC ("TSE"), debtor and the owner of a then defunct ethanol plant in South Dakota, has been ongoing since May of 2003. There are at least eleven matters pending on appeal. Ten appeals are brought by Tri-State Financial, LLC ("TSF"). Some of the orders may well be interlocutory and not appealable as a matter of right. TSF did not seek leave of court pursuant to 28 U.S.C. § 158(a)(3) and claims the district court has jurisdiction pursuant to 28 U.S.C. § 158(a)(1) ("final judgments, orders, and decrees"). No party has challenged jurisdiction. The court intends to consider and decide all pending appeals, if nothing else pursuant to § 158(a)(3). I will deal with all these matters on appeal in an omnibus order and opinion since I am confident that an appeal will be

taken from my order and opinion and I wish to burden the Court of Appeals with as few appeals as possible.

[¶2] This court reviews the legal conclusions of the bankruptcy court *de novo*; findings of fact are upheld unless clearly erroneous. *Wegner v. Grunewaldt,* 821 F.2d 1317, 1320 (8th Cir. 1987) (*citations omitted*). Federal Rule of Bankruptcy Procedure, § 8013 provides as much and tells us that "due regard shall be given to the opportunity of the bankruptcy court to judge the credibility of the witnesses." A finding is clearly erroneous when the reviewing court is left with the definite and firm conviction that a mistake has been committed, this despite the fact that there is some evidence to support the finding. *Anderson v. City of Bessemer,* 470 U.S. 564, 573 (1985), *citing United States v. United States Gypsum Co.,* 333 U.S. 364, 395, 68 S.Ct. 525, 542, 92 L.Ed. 746 (1948).

RECUSAL OF BANKRUPTCY JUDGE

[¶3] On June 30, 2006, TSF filed a motion for a United States Bankruptcy Judge to recuse from any additional proceedings in the bankruptcy case. I will first deal with this matter.

[¶4] 28 U.S.C. § 455(a) provides that a judge "shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned." The question is whether the impartiality of the judge "might reasonably be questioned by the average

person on the street who knows all of the relevant facts." *In re Kansas Public Retirement System,* 85 F.3d 1353, 1358 (8th Cir. 1996) (citations omitted). The existence of "actual bias" need not be shown. *Moran v. Clarke,* 296 F.3d 638, 648 (8th Cir. 2002) (*en banc*), *citing Liljeberg v. Health Servs. Acquisition Corp.,* 486 U.S. 847, 859-60, 108 S.Ct. 2194, 100 L.Ed.2d 855 (1988). 28 U.S.C. § 455(b) provides that a judge "shall also disqualify himself . . . (1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding . . . "

[¶5] The impartiality of a judge is presumed to exist; a party seeking recusal bears a substantial burden to prove otherwise. *United States v. Denton,* 434 F.3d 1104, 1111 (8th Cir. 2006), *citing Lunde v. Helms,* 29 F.3d 367, 370 (8th Cir. 1994). Whether to recuse is committed to the bankruptcy court's sound discretion. *Dossett v. First State Bank,* 399 F.3d 940, 953 (8th Cir. 2005), *citing Moran,* 296 F.3d at 648.

[¶6] The disqualification of a judge for personal bias or prejudice under 28 U.S.C. § 455 is at least somewhat limited by the "extrajudicial source doctrine." *Liteky v. United States,* 510 U.S. 540 (1994). "All of these grounds are inadequate under the principles we have described above: They consist of judicial rulings, routine trial administration efforts, and ordinary admonishments (whether or not legally supportable) to counsel and to witnesses. All occurred in the course of judicial proceedings, *and* neither (1) relied upon knowledge acquired outside such proceedings nor (2)

displayed deep-seated and unequivocal antagonism that would render fair judgment impossible." *Id.* at 556. There is nothing in the record to even suggest bias stemming from any extrajudicial source. Of course, any judge presiding in a given case reaches opinions about parties and counsel. The bankruptcy judge readily concedes that he has done that here. Reaching such opinions would especially be true when the case is so extremely protracted and so bitterly fought at every stage as this case has been. The judge reaches opinions about conduct and occasionally acts to prevent misconduct or miscarriages of justice. That is the nature of being a judge. There is in this case no actual deep-seated antagonism. Nor is there any such antagonism that is "unequivocal." At best, all comments are subtle and equivocal. They are insufficient to show any degree of deep-seated antagonism.

[¶7] TSF "must allege specific, non-conclusory facts showing a personal bias or prejudice against [it] that emanates from an extrajudicial source as distinguished from a judicial source, i.e. court proceedings." *United States v. Kirkpatrick,* 2005 WL 2989314, *citing Youn v. Track, Inc.,* 324 F.3d 409, 423 (6th Cir. 2003). The essence of the complaints of TSF is that the opinions of the bankruptcy judge show a bias against TSF and one of its attorneys. "Adverse judicial rulings, however, 'almost never' constitute a valid basis or recusal; the proper recourse for a dissatisfied litigant is appeal." *Dossett,* 399 F.3d at 953, *citing Liteky,* 510 U.S. at 555.

[¶8] The job of a trial judge is often frustrating, especially when counsel do not act in a professional manner. We are dealing here with a non-jury proceeding. There was no jury to listen to the judge speak about counsel or a party. A judge must, as we all know, be especially careful in the presence of a jury to say and do nothing to influence the jury as to how to decide a case. We know that judicial remarks and comments that are critical or disapproving, or even hostile to, a party or counsel, or to a party's case, ordinarily do not support a motion to disqualify a judge for personal bias or prejudice. *Liteky,* 510 U.S. at 555. In motions hearings or a trial to the court, most judges do not sit like bumps on a log. They express opinions, although in a preliminary fashion until the judge is ready to rule. Judges often question where the lawyers and the parties are going and the arguments being made. They are not required to listen to evidence that is "going nowhere." It is helpful to lawyers to know what the judge is thinking, at least on a preliminary basis, so that the lawyer can correct the judge or change course to meet the questions being raised by the judge. It is part of the process of "trying to get it right."

[¶9] We know also that "even though § 455 has no express timeliness requirements, claims under § 455 will not be considered unless timely made." *In re Kansas Public Employees Retirement System,* 85 F.3d at 1360, *citing Holloway v. United States,* 960 F.2d 1348 (8th Cir. 1992). In that case, a petition for a writ of mandamus (attempting to disqualify a federal

judge) was untimely since it was filed more than one year after the petitioner first learned the claimed relevant facts underlying the motion. 85 F.3d at 1360-61. I will later discuss the timeliness factor in this case.

[¶10] The bankruptcy judge denied the motion for recusal and issued a very lengthy memorandum opinion (117 pages). He sets forth the long history of motions and hearings and what has transpired in this case. The bankruptcy judge treated the motion for recusal very carefully and in great detail. That would be appropriate since no judge wants any litigant or spectator to reach the reasonable opinion that the judge has been unfair or is biased. A judge should be very careful to explain why recusal is not appropriate, assuming that is the case. The bankruptcy judge sets forth that he has been a trial court judge for more than 30 years, including over 18 years as a bankruptcy judge. He describes this case as "one of the more difficult ones over which he has presided, not because of its legal complexity but due to the sheer volume of contested matters and the animosity among major parties." I do not intend to repeat all the matters contained in the memorandum opinion of the bankruptcy judge. It is a very thorough and carefully set out opinion.

[¶11] TSF has taken appeals from the order denying the motion to recuse. The appeals have been filed in CIV 06-1040, CIV 06-1043, and CIV. 07-1003. This is a belt and suspenders approach.

[¶12] TSF has not only sought to require the recusal of the bankruptcy judge but has also alleged that the recently appointed bankruptcy judge in South Dakota should, at the outset, not be allowed to take over the case if the now retired bankruptcy judge is recused. TSF suggests that we need a bankruptcy judge from Iowa. This is a collateral gratuitous improper attack on the integrity and fairness of the recently appointed bankruptcy judge for the District of South Dakota. TSF has accused the now retired bankruptcy judge of twice lying, of conducting kangaroo court proceedings, of improperly giving documentary evidence to a bankruptcy judge from the District of Minnesota (also accusing the Minnesota judge of improperly looking at the documentary evidence), of disliking the principal investor in TSF because of his wealth and because he allegedly made unwanted sexual comments to a member of the judge's staff, of disliking the *pro hac vice* TSF attorney, and attempting to put that attorney "in his place", given the fact that the attorney is a former bankruptcy judge from Nebraska.

[¶13] TSF and its attorneys filed and endorsed an affidavit from a part time reporter for a weekly newspaper in Rosholt, S.D., the very small town in which the ethanol plant is located. TSF admits in a brief (page 10 of Doc. 59 in CIV 06-1040) that TSF procured the affidavit in question. It is well known that most affidavits in every case are drafted by an attorney. There is no doubt that TSF and its attorneys obtained this affidavit and used it in a filing with the bankruptcy court and again in the district

court. The affidavit is scandalous. It states opinions and conclusions rather than facts. It claims that the court proceedings "were an exercise in gamesmanship," that the bankruptcy judge's threat to continue hearings "bordered on blackmail", that the bankruptcy judge engaged in "legal gymnastics", that the judge was "favoring the Australians", that attorney Lovald (the trustee) and his attorney were acting improperly and were "only doing what the judge told them to do", that the proceedings were conducted as a "kangaroo court", and that unnamed people in Rosholt would be unhappy with the rulings of the bankruptcy judge. TSF has thus also charged the trustee with unethical conduct and not fulfilling his independent obligations as an attorney but being, in effect, under the thumb of the bankruptcy judge. TSF also charges that the trustee has violated his fiduciary responsibilities. TSF has made the same accusations against one of the attorneys for the trustee, a well respected attorney and past president of the State Bar of South Dakota. TSF has also challenged the award of fees to the attorney for the trustee, claiming that he had acted under a conflict of interest. This matter of fees is a separate appeal which I will address later in this order and opinion.

[¶14] The motion for recusal was filed in violation of local rules since it was not signed by local counsel for TSF. It should have been denied on that basis alone. The *pro hac vice* attorney and TSF continue to insist it was signed by local counsel. It was filed electronically and shows only s/ before the typed name of the

pro hac vice attorney. The correct procedure was and is to show /s/. There is no signature line for the then local counsel for TSF and no s/ or /s/ before the typed name of the local counsel to meet the requirements of the local rules on electronic filing. What the practices were at the time of the filing and what the requirements have been since electronic filing was implemented in the District of South Dakota are now explained in D.S.D.LR 5.4 (although the entire version of all the new rules was not effective until March of 2007). In other words, the rule then is the same as the rule today. I have looked specifically at what was filed in BK 03-10194. The contentions of TSF and their attorneys are rejected. Many other filings by the TSF attorneys show that they were fully aware of the requirements for electronic signatures. I will nevertheless deal with the motion on its merits, as did the bankruptcy judge.

[¶15] A former accountant for TSE and perhaps TSF, who was also a member of the board of managers of TSE, James Jandrain, through his attorney, joined in the motion for recusal. The history, in part, as to Mr. Jandrain, is set forth in paragraph 28 of the affidavit of the trustee. Mr. Jandrain has had significant conflicts of interest in sitting on the board of managers of TSE, then claiming to act at the same time as the corporate accountant, and acting on behalf of TSF as a member. Mr. Jandrain felt unfairly treated because his claim for more than $50,000.00 for claimed services as a certified public accountant for the debtor was rejected by the bankruptcy judge

after a hearing. This action was the source of an earlier appeal to this court which I found to be without merit and which I remanded to the bankruptcy court.

[¶16] ICM, Inc. and Randy Kramer (Kramer, at one time the president of TSE, now a member of TSF and thus hardly a disinterested person, is represented by an attorney who also represents James Jandrain) filed pro forma joinders in the motion for recusal. TSF filed objections to a settlement between the trustee and Murphy Brothers. The objection was based, at least in part, on the failure of the settlement to cause $82,996.00 to be paid to Randy Kramer. TSF is obviously representing or attempting to represent the interests of Randy Kramer.

[¶17] TSF filed, in connection with the motion for recusal, a motion for leave for TSF to depose the trustee. This motion was referred by the bankruptcy judge (because the bankruptcy judge had not yet ruled on the recusal motion) to Robert Bankruptcy judge. [sic] Kressel, United States Bankruptcy Judge for the District of Minnesota. Judge Kressel denied the motion. TSF then filed a motion to reconsider both the order of the South Dakota bankruptcy judge referring the motion to Judge Kressel and the ruling of Judge Kressel on the motion. TSF, without doing any research, challenged the legal authority of Judge Kressel to act, ignoring the fact that the Chief Judge of the United States Court of Appeals for the Eighth Circuit had, on December 7, 2005, entered an order designating Judge Kressel to act in connection with

South Dakota bankruptcy matters. Judge Kressel denied the motion for reconsideration.

[¶18] TSF has now filed in this court, among other things, an appeal from (1) the Order Transferring Case for Purpose of Ruling on Motion for Leave to Take Deposition, and (2) Order Denying Motion to take Deposition. These have been filed in the three civil files listed above.

[¶19] The motion for reconsideration should not have been filed, in any event. TSF cited no authority which would permit, much less require, a reconsideration. The Federal Rules of Civil Procedure do not allow a "motion to reconsider." *See Humphreys v. Roche Biomedical Laboratories, Inc.*, 990 F.2d 1078, 1081 (8th Cir. 1993), and *In re Trout*, 984 F.2d 977, 978 (8th Cir. 1993) (warning counsel that the Federal Rules of Civil Procedure do not provide for a motion for reconsideration and directing counsel to properly designate a motion under the rule authorizing the motion). The process of seeking reconsideration could be transformed into an endless chain of motions, filing a motion to reconsider the denial of the motion to reconsider, *ad infinitum*. As now Chief Judge Loken observed in his opinion in *Wilkins v. Hartford Life and Accident Insur. Co.*, 299 F.3d 945, 948 (8th Cir. 2002): "Such motions (to reconsider) are frequently a futile waste of time for both the parties and the trial court." *See also Broadway v. Norris*, 193 F.3d 987, 990 (8th Cir. 1999) (Rule 60(b) motion is not for purpose of rearguing, somewhat more fully, merits of claim). I realize, of course, that the parties in a

bankruptcy proceeding are governed largely by the Bankruptcy Rules, including Rule 9024 (which would not allow a motion for reconsideration of a motion dealing with a deposition and which refers to Fed.R.Civ.P. 60(b)). I believe the principles set forth above apply in bankruptcy proceedings.

[¶20] The record is replete with the extreme and continuous litigiousness of TSF and its *pro hac vice* attorney. The various unauthorized motions for reconsideration are simply additional evidence of that.

[¶21] As further evidence of improper conduct by TSF and its attorneys, TSF filed on September 11, 2006, what was called "Motion to Reconsider, Alter and/or (sic) Amend Decision." I have already discussed the matter of motions to reconsider which are not authorized by any rule. In addition, attorney Strasheim filed the motion without the signature of local counsel, in violation of a local rule, 83.2(E). The South Dakota judge ordered the motion stricken from the record and denied it.

[¶22] TSF has now also taken appeals from (1) Judge Kressel's Order Denying Motion to Reconsider, Set Aside, Alter and/or (sic) Amend Orders, (2) the South Dakota judge's Order Striking Motion to Reconsider, Alter and/or (sic) Amend Orders, and (3) the Order to set Deadlines. Appeals are pending in the three civil files described above.

[¶23] An unsecured creditor, Eugene Paulson, filed his response in BK No. 03-10194, setting forth what

he had observed about the conduct of John Hoich, the principal investor in TSF, and what he had observed about the part-time reporter for the Rosholt newspaper. Although filed beyond the deadline set by the bankruptcy judge. Mr. Paulson opposed the recusal motion and explained why.

[¶24] The largest creditor, First Dakota National Bank ("First Dakota"), objected to the recusal motion, stating that " ... TSF has been extraordinarily litigious, difficult to deal with and otherwise counterproductive throughout the Chapter 7 process." First Dakota points out how detrimental it would be to have the bankruptcy judge removed after presiding over this bankruptcy case for more than three years, that TSF has been treated fairly and in some instances, very favorably, by the judge, and that, of all the hundreds of creditors in this case, only TSF (and those in privity with TSF) think the judge should recuse. First Dakota concedes that the judge has often been frustrated by the continuous objections (even after rulings) and methods of operations of TSF and its attorneys. the [sic] bankruptcy judge has expressed on the record how frustrating it has been to preside over a case in which TSF and its attorneys have treated the judge and the other parties so poorly.

[¶25] We know that TSF and the entity, American Prairie Construction Company, f/k/a North Central Construction, Inc., ("NCC") that built the ethanol plant in question, reached a settlement in the presence of the bankruptcy judge which was on the record

in June of 2004. This was followed by TSF reneging on the settlement by adding terms not previously stated. The bankruptcy judge did not enforce the settlement and allowed TSF to escape from it. Of course, this would be frustrating to any judge.

[¶26] TSF and NCC later went to a mediation session before United States Magistrate Judge John Simko. Again, an oral settlement (on the record, however) was reached before Judge Simko in July of 2005. Judge Simko reported to the bankruptcy judge, as is the universal practice of Judge Simko, that a settlement had been reached by TSF and NCC, and the bankruptcy judge cancelled a hearing set for August 29, 2005. Again, TSF later backed away. The TSF attorney argued subject matter jurisdiction of the bankruptcy court to enforce any settlement and argued that he and TSF would not recognize the record made at the conclusion of the mediation session on July 26, 2005, as being the best record of the "core agreements" reached that day. I am unclear as to whether the claim is that the court reporter acted improperly or failed to "take down" what was said. In any event, the bankruptcy judge did not enforce this settlement as well and did not look at the transcript until it was unsealed.

[¶27] TSF took another earlier appeal to this court on February 23, 2006. I dismissed that appeal on April 12, 2006, finding that the appeal was "totally without merit" and that I had no jurisdiction over the bankruptcy court's interlocutory order regarding the mediated settlement. The appeal of TSF to the

district court was frivolous. TSF appealed my ruling to the United States Court of Appeals for the Eighth Circuit on April 27, 2006, and dismissed the appeal by motion on May 22, 2006. Such second appeal was also frivolous as a matter of law.

[¶28] NCC has also opposed the motion to recuse. NCC points out that TSF ultimately settled with the trustee which settlement was approved by the bankruptcy judge. Only after such beneficial ruling did TSF file the recusal motion.

[¶29] TSF makes much of the judge's strong criticism of TSF, its related parties, and others who had proceeded during the bankruptcy proceeding to retrofit the ethanol plant at considerable expense, all without court approval and, in fact, after the bankruptcy judge had refused on December 12, 2003, to approve the expenditures for the retrofitting. TSF, the debtor, and others conferred in private after the judge had refused to allow retrofitting (with TSF to receive a super priority status). These people made the decision to proceed without approval and actually in the face of disapproval. TSF and its present attorneys blame that decision on the former lawyer for TSF. TSF is, of course, responsible for what its lawyer does or does not do. Any judge would be bothered by parties and lawyers doing end runs on the court and the court's previous rulings. Yet the bankruptcy judge, prior to the recusal motion being filed, approved a settlement with TSF that will result in the retrofitting expenses being covered. In short, TSF and

its lawyers "got away" with the end run and have no valid complaint about the matter.

[¶30] The bankruptcy trustee also filed a lengthy objection to the motion for recusal. In support, the trustee filed a very detailed and comprehensive affidavit which rebuts point for point the allegations of TSF and sets forth the protracted nature of the proceedings in bankruptcy court. The affidavit makes it clear that the unhappiness of TSF stems largely from not being permitted by the trustee and the bankruptcy judge to be the sole bidder to buy the ethanol plant. Had the judge permitted this, there would have been great detriment to unsecured and other creditors. As a result of the actions of the judge and the trustee, it appears that all creditors may be paid in full.

[¶31] TSF argues, without any citation of authority, that the trustee is not an appellee and has no standing in these appeals. The claim of TSF that the trustee has no legitimate interest in whether or not the bankruptcy judge is forced to recuse in a case that is now more than three years old makes no sense. Bringing in a new judge would greatly prolong the case and result in much delay, all to the detriment of the creditors. The trustee in his representative capacity would be subject to great injury and would be aggrieved by what would result if TSF were to be successful in its motion for recusal. TSF argues that the trustee should have filed a notice of appeal. The question would be: appeal from what? TSF also argues that the trustee should have filed a notice of

cross appeal. The question would be: cross appeal from what? I reject the arguments of TSF as to the trustee. The arguments and positions of the trustee are all a matter of record in the bankruptcy court and nothing is added by what is filed in the district court.

[¶32] The trustee sets forth in paragraph 30 of the affidavit that TSF "continues to file multiple objections in an attempt to delay the Chapter 7 Estate in making an ultimate distribution to unsecured creditors in this case." That is no doubt true. It is no doubt true that TSF objects to virtually everything in the bankruptcy court and appeals virtually every ruling of the bankruptcy court to the district court. Of course, any party has the right to appeal to a higher court but this does not permit objections or appeals which are frivolous.

[¶33] The trustee calls some of TSF's comments in connection with the recusal motion "reckless and misleading." He calls TSF suggestions "a red herring." He slates that TSF "has every intention of delaying the administration of this estate for the foreseeable future." I agree. The record reflects this and there can be no other logical explanation for the actions of TSF and its attorneys.

[¶34] The trustee reached a settlement agreement (subject to court approval) with NCC. TSF has objected to that and a contested hearing will be required and perhaps already has been conducted by the retired bankruptcy judge.

[¶35] Trustee Lovald states in his affidavit that TSF "has been and continues to be engaged in a bitter vendetta with this creditor (i.e. NCC) and appears to want to use the estate, and the estate's resources, to continue the dispute unabated. That course of action could tie up the estate for years to come, and substantially reduce the estate's cash, because of the priority position held by North Central Construction." The trustee also states under oath: "Trustee respectfully submits that the Motion for Recusal submitted by Tri-State Financial is nothing more than a thinly veiled and stale attempt to judge shop in an attempt to dominate and control all decisions in the administration of this case, and to hijack the estate's limited resources to engage in endless litigation with North Central Construction, and should be summarily denied."

[¶36] TSF attempts to rely on *United States v. Pfizer, Inc.*, 560 F.2d 319 (8th Cir. 1977), a case in which a then United States District Judge in Minnesota decided to force the parties into a trial to the court based upon his belief that the case was too complicated for a jury trial. He did so after forming strong opinions and after actively and aggressively attempting to force the parties to settle. He even expressed his opinion before the scheduled trial on the monetary value of the claims. In the present case, the bankruptcy judge took no part in the settlement discussions or the expressions by the parties, including TSF, that a settlement had been reached. He naturally was displeased when the parties claimed

(once in the presence of the bankruptcy judge and once in the presence of Judge Simko) to have reached a settlement, only to then have the "settlement" fall apart twice. Delays and confusion were caused by these activities and no judge appreciates such diversions. *Pfizer* has no relevance to the case now before this court.

[¶37] I will return to the issue of timeliness of the recusal motion. The complaints of TSF stem largely from the judge's decision to convert this case from a Chapter 11 case to a Chapter 7 case in July of 2004 and the manner in which the bidding process (to sell the ethanol plant) was conducted in October of 2004. These actions took place more than 20 months before the recusal motion was filed. TSF knew long ago that the judge was very unhappy about what had transpired as to the unauthorized retrofitting of the plant. He was unhappy about the insider machinations between and among TSE, TSF and others. He was unhappy with the conduct of TSF officials and its attorneys during the bankruptcy proceedings. The bankruptcy judge thought the credibility of witnesses presented by TSF was poor. Any judge has the right to reach those opinions. TSF knew about all these matters long ago. They certainly knew about them on July 28, 2004, by their own admission. The TSF complaints about the comments of the bankruptcy judge on May 4, 2006, that, although he was retiring, he intended to retain this case, are much ado about nothing and are no evidence of bias or perceived bias. There is no evidence that the comments were

addressed to anyone in particular. The motion is, as a matter of law, untimely, at least as to perceived bias. On the basis of untimeliness alone, the ruling of the bankruptcy judge on the recusal motion should be affirmed.

[¶38] In addition, I agree with all the sworn statements of trustee Lovald as set forth above and the record fully supports the statements. I find and conclude that, based on the record before the court, the recusal motion was not made in good faith but for the improper purpose of further delay and harassment of the trustee, other attorneys, creditors, and the judges. I find and conclude that the impartiality of the bankruptcy judge may not be "reasonably" questioned. Nor would the average person "on the street" who knows all the facts reasonably question such impartiality.

[¶39] TSF complains that the bankruptcy judge asked for views of counsel as to whether he should recuse. There is no evidence of this and TSF cites to no portion of the record to support the claim. The judge did set a deadline for joinders and other responses. TSF's allies took advantage of that and filed joinders. I agree that a judge considering recusal should not ask for the views of the attorneys, at least unless there is a procedure for responses to be filed which are not available to the judge. Again, there is no evidence that the judge did anything other than allowing responses and joinders. If there was any error, it was harmless.

[¶40] I find and conclude that the bankruptcy judge acted properly and objectively within his discretion in deciding to deny the motion to recuse. His order of September 1, 2006, should be affirmed. This will cover the appeals of this issue in CIV 06-1040, CIV 06-1043, and CIV 07-1003.

[¶41] TSF and its attorneys have pursued the same course of conduct (displayed in the bankruptcy court) in the district court. In their initial brief, they filed an over length brief in violation of then D.S.D.LR 7.2(B). The brief also was filed in violation of the professional obligations of members of the bar. It contained scandalous material filled with many scurrilous accusations against the bankruptcy judge, other judges, and attorneys involved in this case. I ordered the brief stricken and to be filed under seal to facilitate appellate review. I filed an extensive order and opinion (Doc. 37 in CIV 06-1040) which I incorporate by reference in this Order and Opinion. The brief (Doc. 10-1 in CIV 06-1040) illustrates the methods of operation employed by the *pro hac vice* attorney and his client in this entire matter. As I have at least intimated earlier, I have never seen anything like it in all the years I have been admitted to practice (since 1962).

[¶42] I filed another Order and Opinion (Doc. 45 in CIV 06-1040) on February 2, 2007. I ruled on a TSF motion (Doc. 21 in CIV 06-1043, no comparable motion having been filed in CIV 06-1040). I set forth in such Order and Opinion that counsel for TSF were trying to "set up" the district court by filing a motion

asking the court to direct what material could be included in a TSF brief covering one of the issues on appeal. Of course, no responsible judge would do anything of the kind. I also set forth that counsel for TSF had engaged in "a blatant misstatement of the record." I continue to adhere to that finding and conclusion.

[¶43] To further show the depths to which this case has sunk, the trustee filed motions to disqualify the *pro hac vice* counsel in these various cases. The trustee also filed motions seeking an award of attorney fees and costs against this attorney for the claimed misconduct of the TSF attorneys. On April 23, 2007, I entered an Order and Opinion (Doc. 60 in CIV 06-1040 and Doc. 52 in CIV 06-1043) referring what I believed was a request for disciplinary action to Chief Judge Schreier. The referral was pursuant to D.S.D.LR 83.2(G)(2). This includes the motions to disqualify and the motions for sanctions. I have never previously seen a motion seeking to remove *pro hac vice* counsel from participation in a case.

[¶44] The Nebraska attorney through a South Dakota attorney (who has since been replaced as local counsel) sought *pro hac vice* admission in another case (CIV 07-1003) and I have not granted the motion. The non-admitted attorney once again signed the notice of appeal (as he has done in all the other appeals) although he had not at the time of signing been admitted to practice. These actions would be additional violations of the rules of practice.

APPEALS FROM SIX OTHER BANKRUPTCY COURT ORDERS

[¶45] I will turn now to the appeals of TSF from another six interlocutory orders. The notice of appeal (Doc. 1) in CIV. 07-1003 describes them. Appeals are also taken from the same six other interlocutory orders in CIV 06-1040 and CIV 06-1043.

[¶46] All appeals of the Order Transferring Case for Purpose of Ruling on Motion for Leave to Take Deposition are entirely frivolous, as I have discussed previously in this opinion. The bankruptcy judge had the authority to transfer the pending motion and Judge Kressel had the authority to rule on the motion and did so. Such Order should be affirmed.

[¶47] All appeals of the Order Denying Motion to Take Deposition (of the trustee) should be rejected as clearly within the discretion of Judge Kressel, which discretion was properly exercised. The record here is more than complete. Taking the deposition of attorney and trustee Lovald would have been nothing but a source for more indigestion and bad blood between counsel. The Order should be affirmed. TSF attempts to broaden the issue before the court to include the claimed "right to discovery." Nothing was before the bankruptcy court other than a request to be permitted to depose the trustee. That is the issue before this court on appeal.

[¶48] All appeals of the Order Denying Motion to Reconsider, Set Aside, Alter and/or (sic) Amend Orders are entirely frivolous, not permitted by either

the bankruptcy rules or the Federal Rules of Civil Procedure, and the Order entered by Judge Kressel should be affirmed.

[¶49] All appeals of the Order Striking Motion to Reconsider, Set Aside, Alter and/or (sic) Amend Orders are also frivolous, the motion having been made in violation of local rules (i.e. not signed by local counsel), not permitted by either the bankruptcy rules or the Federal Rules of Civil Procedure, and the Order should be affirmed.

[¶50] All appeals of the Order to Set Deadlines are also clearly within the discretion of the bankruptcy judge which discretion was properly exercised; the Order should be affirmed.

APPEAL FROM ORDER APPROVING FEES OF TRUSTEE'S ATTORNEY

[¶51] I turn next to what is yet to be decided in CIV 06-1040. Although the notice of appeal includes all orders described above, it also deals with an appeal by TSF of an order of the bankruptcy court approving an application for fees and expenses to the attorney representing the trustee. Once again, the Nebraska attorney signed the notice of appeal without being admitted *pro hac vice* in this case. It would seem to be elementary to not do so. TSF filed a 53 page brief, in violation of the local rules which permit only 25 pages unless authorized in advance by the judge. Among other things, TSF alleged that the judge should not, apparently because of the motion for recusal, have

ruled on the fee application of the trustee's attorney. In the alternative, TSF alleges that the application for fees should have been denied. TSF alleges that the appointment of the attorney by the bankruptcy judge was invalid, that the attorney had a conflict of interest in representing an interest adverse to the Chapter 7 estate, that the attorney lacked candor and failed to make a complete disclosure, that the trustee and his attorney knew of the conflict and ignored it, that the alleged waiver of the conflict by the trustee and the attorney (which would seem to fly in the face of the allegation that the trustee and the attorney ignored the conflict) was of no legal effect, and numerous other allegations. The essence of the TSF claim is that the attorney for the trustee represented the Clapper Corporation which held a disputed claim of $195,929.43 at the same time that the attorney represented the trustee. An amended claim was later filed, reducing the Clapper claim to $95,630.29. TSF objected to the claim for fees and costs on the same day TSF filed the recusal motion. The bankruptcy judge overruled the TSF objections and approved the fee application.

[¶52] The TSF brief includes a great deal of material having absolutely no relevance to the fee application questions. The brief moves back and forth from one subject to another. The brief attempts to raise unrelated claims on behalf of ICM (who allegedly was forced by the judge to buckle under), James Jandrain, TSE, and Randy Kramer. The TSF attorney attempts several times to become a witness in the brief. TSF

rehashes in extensive detail what took place in connection with the efforts to sell the ethanol plant, setting forth that TSF paid $27,900,000.00 for the TSE assets and complains that TSF paid too much. That would seem to be a benefit to the creditors. If TSF paid "too much" pursuant to a settlement, this is not something that can be rectified by this court. All of this, in any event, took place in 2004, a long time ago. TSF raises numerous non-issues which pre-dated the settlement reached by TSF with the trustee. The settlement by the parties moots the complaints of TSF about the process that took place before the settlement.

[¶53] On August 3, 2004, the trustee filed an application to employ the attorney in question and another attorney from his law firm. The application disclosed that the attorney in question "is counsel for unsecured creditor Clapper Corporation." A claim had been filed by Clapper when this was a Chapter 11 proceeding. Not until the case was converted to Chapter 7 did the trustee approach the attorney about representing the trustee.

[¶54] TSF complains that there was no disclosure of waivers of the conflict of interest. If TSF had some questions about that matter, it should have raised them in 2004, not in late 2006. If TSF was concerned, TSF should have objected to the initial appointment of the attorney but did not do so. Of course, anyone would anticipate that any actual conflicts of interest would be waived or the attorney could not proceed. 11 U.S.C. § 327(c) provides that a person is not

disqualified for employment by the trustee "solely because of such person's employment by or representation of a creditor, unless there is objection by another creditor or the United States trustee, in which case the court shall disapprove such employment if there is an actual conflict of interest."

[¶55] Clearly, the appointment of the attorney by the bankruptcy judge was proper under the facts and the law. The initial disclosure by the attorney was entirely proper and sufficient. Again, the finding by the bankruptcy judge as to these matters is not clearly erroneous. In fact, it is not erroneous.

[¶56] The trustee later independently contested at least one of the Clapper claims and the dispute is apparently not resolved. The attorney in question did not know that the Clapper claims (one of which arose during the course of the bankruptcy proceeding) would be challenged until long after he was appointed to represent the trustee. The trustee also did not anticipate any actual conflict of interest when the attorney was appointed. The findings of the bankruptcy judge to this effect are not clearly erroneous. The trustee has since employed independent counsel to challenge at least one of the Clapper claims. The attorney in question has at no time represented the bankruptcy estate in connection with the Clapper claims.

[¶57] It is clear that no harm has occurred to anyone at this juncture. Certainly no financial harm has occurred to anyone. This includes TSF. The trustee

and his attorney could have perhaps been more careful when it appeared that an actual conflict of interest had developed, bringing it to the specific attention of the bankruptcy judge and the other parties. This, however, is not sufficient to deny the attorney the compensation to which he is clearly entitled.

[¶58] There is no evidence that the trustee or his attorney should have been able to anticipate an actual later dispute over the Clapper claim. There is no justification for TSF raising no questions or objections until after the attorney had performed valuable services for the trustee. TSF has "laid in the weeds" and it would be highly inequitable to punish the trustee's attorney in the manner sought by TSF. TSF admits that the attorney "performed a wide range of services" for the trustee, including representing the trustee in the "sale and disposition of the assets of TSE and in opposing some claims and paying some claims." TSF does not deny that the fees are reasonable, the sole objection being the result of the conflict of interest. TSF in fact relied on the attorney to present the settlement (between TSF and the trustee) to the bankruptcy judge and obtain his approval. The objections to the fees of the attorney and the appeal of the matter only further demonstrate the "bad blood" that exists throughout this bankruptcy case. The order of the bankruptcy judge approving the fees on October 19, 2006, should be affirmed.

APPEAL AND CROSS APPEAL AS TO PREPAYMENT PENALTY

[¶59] TSF has appealed from the bankruptcy court's decision to allow the recovery by First Dakota National Bank ("First Dakota") of a prepayment penalty of $173,253.27 plus interest from May 23, 2003, until paid, from the bankruptcy estate as a pre-petition liability, i.e. existing prior to the bankruptcy filing on May 23, 2003. The bankruptcy court thus held that the prepayment penalty was due First Dakota as a component of the secured claim of First Dakota, this pursuant to 11 U.S.C. § 502(b). First Dakota had sought by motion the payment of the prepayment penalty (2% of the remaining balance on the loan) as a post-petition liability of the estate, this pursuant to 11 U.S.C. § 506(b). Both TSF and the trustee objected to the motion. TSF claims that the bankruptcy judge could not rule in favor of First Dakota on a theory not advanced by the debtor. That contention should be rejected. While it is true that the bankruptcy court awarded relief to First Dakota, not under the relief sought by First Dakota (11 U.S.C. § 506(b) but under 11 U.S.C. § 502(b)), the bankruptcy judge acted within his discretion in deciding a case based on an issue not raised by a party.

[¶60] First Dakota filed a cross appeal to this court from the ruling that denied it recovery under 11 U.S.C. § 506(b). Obviously, First Dakota does not seek a double recovery of the prepayment penalty but filed the cross appeal to protect its rights. There are fundamental differences between 11 U.S.C. § 506(b) and

§ 502(b). Federal law and not state law determines what may be recovered under § 506(b). *In re Schriock Construction, Inc.,* 104 F.3d 200, 202-03 (8th Cir. 1997). By contrast, under § 502(b)(1), pre-petition claims must be disallowed if unenforceable under state law. It is not surprising that First Dakota would choose to proceed under § 506(b).

[¶61] The debtor, TSE, had defaulted on loan payments due First Dakota. On May 16, 2003, First Dakota filed an action in state court to foreclose its mortgage on the TSE ethanol plant. First Dakota alleged that it had accelerated the amounts owing on two notes and that the "entire principal, accrued interest, and other amounts owed" First Dakota "was immediately due and payable." No allegations were specifically made about any prepayment penalty being claimed or sought. The general allegations, however, would clearly be sufficient under the modern rules of pleading.

[¶62] As previously stated, TSE filed a Chapter 11 bankruptcy case on May 23, 2003. On July 29, 2004, the case was converted to a Chapter 7 case. The trustee sold the ethanol plant in 2005. Pursuant to a bankruptcy court order of February 15, 2005, the trustee paid First Dakota from the sale proceeds all principal, interest to the date of payment, and most of the attorney's fees and costs owing on the two notes. The trustee did not pay the First Dakota claimed prepayment penalty or attorney fees associated with the prepayment penalty.

[¶63] The business loan agreement ("BLE") entered into by TSE and First Dakota on May 14, 2001, provides, in part: "B) Prepayment. A prepayment charge of 2% on any unscheduled principal payments for the first seven years of the term loan in excess of the aforementioned free cash flow." As the bankruptcy judge noted in his opinion, this is not a sentence. It is found under this section: "NEGATIVE COVENANTS. Borrower covenants and agrees with Lender that while this Agreement is in effect, Borrower shall not, without the prior written consent of Lender:"

[¶64] There is a large section of the BLE dealing with "DEFAULT." Nothing is mentioned in that section as to any required prepayment penalty in the event of default. There is a very large section of the BLE dealing with "DEFINITIONS." There is no definition of "prepayment." The BLE clearly provides that it is governed by the laws of the State of South Dakota.

[¶65] A promissory note for $9 million was executed that same day and the loan was made. Payment in full was required on February 14, 2002. One of the provisions of that note was: "PREPAYMENT: MINIMUM INTEREST CHARGE . . . In any event, even upon full prepayment of this note, Borrower understands that Lender is entitled to a minimum interest charge of $50. Other than Borrower's obligation to pay any minimum interest charge, *Borrower may pay without penalty all or a portion of the amount owed earlier than it is due.* Early payments will not, unless agreed to by Lender in writing, relieve Borrower of

Borrower's obligation to continue to make payments under the payment schedule. Rather, early payments will reduce the principal balance due" (emphasis supplied).

[¶66] The note also provided: "LENDER'S RIGHTS. Upon default, Lender may declare the entire unpaid principal balance on this Note and all accrued unpaid interest immediately due, *and then Borrower will pay that amount*" (emphasis supplied). There can be no doubt that "that amount" would be the unpaid principal and all then accrued unpaid interest. Nothing was provided about the prepayment charge also being due or included within "that amount." If that was the intent of the parties, it would have been simple to say so.

[¶67] There is no ambiguity in these provisions of the note. The language is clear. Parole evidence would not be admissible and should not have been admitted by the bankruptcy court.

[¶68] Next, there was a loan modification agreement dated February 6, 2002. The maturity of the promissory note of May 14, 2001, was extended until March 15, 2002. The principal balance is recited to be $8,417,089.97. The modification agreement recites: "This loan will have a 2% prepay if paid from proceeds other than by renewal with a First Dakota term loan."

[¶69] It is obvious that this last-quoted provision has no legal effect because, on March 15, 2002, a replacement promissory note was executed and

delivered. This shows the debt at $9 million and the maturity date became March 1, 2012. This final version of the note (and the note which must be used, at least in part, to answer the questions here) provided for 117 monthly consecutive principal and interest payments of $117,700.00 each, beginning June 1, 2002, with interest at 9.500% per annum, and one principal and interest payment of $118,336.20 on March 1, 2012, with interest calculated on the unpaid principal balances at an interest rate of 9.500% per annum.

[¶70] The replacement note provided, as did the previous version: "PREPAYMENT: MINIMUM INTEREST CHARGE . . . In any event, even upon full prepayment of this note, Borrower understands that Lender is entitled to a minimum interest charge of $50. Other than Borrower's obligation to pay any minimum interest charge, *Borrower may pay without penalty all or a portion of the amount owed earlier than it is due.* Early payments will not, unless agreed to by Lender in writing, relieve Borrower of Borrower's obligation to continue to make payments under the payment schedule. Rather, early payments will reduce the principal balance due" (emphasis supplied).

[¶71] The replacement note also provided: "LENDER'S RIGHTS. Upon default, Lender may declare the entire unpaid principal balance on this Note and all accrued unpaid interest immediately due, *and then Borrower will pay that amount*" (emphasis supplied). There can be no doubt that "that

amount" would be the unpaid principal and all then accrued unpaid interest. Nothing was provided about the prepayment charge also being due or included within "that amount." If that was the intent of the parties, it would have been simple to say so. There is no ambiguity in this provision of the note. The language is clear.

[¶72] The new note also provided: "PREPAYMENT PROVISION. A prepayment charge of 2% on any unscheduled principal payments for the first seven years of the term loan, in excess of the free cash flow. Free cash flow is defined in the Business Loan Agreement dated May 14, 2001." Nothing was provided about the prepayment charge applying in the case of the mortgagee choosing to accelerate the loan to force a pay-off of the loan and all interest. If that was the intention of the mortgagee, it would have been easy to say so. The note again provides that it is governed by the laws of the State of South Dakota.

[¶73] A promissory note was also executed and delivered to First Dakota on November 20, 2002, the consideration being a loan of $600,000.00. This note contains the same language described in the earlier notes under "PREPAYMENT: MINIMUM INTEREST CHARGE" and "LENDER'S RIGHTS." There is no provision in this note dealing with any prepayment charge of 2%. Again, the note is said to be governed by South Dakota law. There is no mention whatsoever of any prepayment penalty.

[¶74] Mortgages secured the loans. Nothing in the mortgage addresses what is to happen upon a prepayment of the debt. However, one provision of the mortgage of March 15, 2002, is as follows: "Accelerate Indebtedness. Lender shall have the right at its option without notice to Grantor to declare the entire indebtedness immediately due and payable, *including any prepayment penalty, which Grantor would be required to pay*" (emphasis supplied). The language does not specifically and clearly require the payment of the prepayment penalty. The reference could well be read to require looking at other documents to see whether there is in fact "any prepayment penalty which Grantor would be required to pay." The language could well be read to require an examination of South Dakota law to determine whether a prepayment penalty could be required upon First Dakota declaring the entire indebtedness immediately due and payable. The language is ambiguous and poorly written. I respectfully disagree with the conclusion of the bankruptcy court that the default language in the mortgage "clearly contemplates" that the prepayment penalty would become due upon acceleration of the debt. I reach the opposite conclusion.

[¶75] Compare, e.g., the language found in an instrument of debt described in *In re Ridgewood Apartments of DeKalb County, Ltd.*, 174 B.R. 712, 721 (Bktcy. S.D. Ohio 1994): "Borrower shall pay the prepayment premium due . . . whether the prepayment is voluntary or involuntary (in connection with Lender's acceleration of the unpaid principal balance

of the Note) or the Instrument is satisfied or released by foreclosure (whether by power of sale or judicial proceeding), deed in lieu of foreclosure or by any other means."

[¶76] There are other problems. The note constitutes the debt. It is elementary that the mortgage secures the note. In the absence of the note, there is no consideration for the mortgage. All of this is elementary. It is possible, despite the ambiguity discussed above, that the mortgage provides for one thing as to the prepayment penalty and the promissory notes do not. In this sense, there is also ambiguity. The bankruptcy court received no evidence as to the intent of the parties other than the intent as to the prepayment penalty. The bankruptcy court received no evidence and made no findings as to any claimed intent of the parties as to whether, assuming the prepayment penalty exists in the abstract, such a penalty was to be applied upon First Dakota accelerating the debt, demanding full payment of all principal and interest due. What the intention of the parties may have been (assuming that any such evidence was admissible, given the clear provisions of the promissory notes) as to a prepayment penalty in the abstract is entirely immaterial. No evidence was received nor was anything decided below about possible unconscionability of the prepayment penalty in the event of the lender accelerating the debt. Ambiguities are construed against the drafter of the instruments, in this case First Dakota. In the normal course, the court would look at the mortgage and the

note as one transaction and construe them together. The notes do not contain any provision incorporating the terms of the mortgage by reference.

[¶77] "The generally accepted rule is stated in 55 Am.Jur.2d Mortgages, § 176, at 303, 304 (1971): Although there is contrary authority, it is a widely accepted general rule that a mortgage or deed of trust and a note or bond secured by it are to be deemed parts of one transaction and construed together as such; the provisions of both should be given effect, if possible, and the intention of the parties as determined from an examination of both, not from one separately, must prevail . . . Where, however, there is an irreconcilable difference between notes or bonds and mortgages or deeds of trust given to secure them, the former control." *Ferguson v. Peoples Nat'l. Bank,* 800 SW2d 181, 183 (Tenn 1990).

[¶78] "Generally, the provisions of a promissory note and a mortgage given to secure payment of the note must be construed together whenever possible." *First Interstate Bank, N.A. v. Rebarchek,* 511 NW2d 235, 241 (ND 1994), *citing Lakeland Realty Co. of Minnesota v. Reese,* 46 NW2d 696 (N.D. 1951), and *Interstate Finance Corporation v. Brink,* 6 NW2d 120 (Iowa 1942). "However, when there is an irreconcilable conflict between the terms of the note and mortgage as to maturity, the terms of the note must prevail because the note is the principal obligation and the mortgage only incidental to it." (citing cases) *Id.*

[¶79] The question then becomes: is there irreconcilable conflict between the terms of the promissory notes and the mortgage? This is not a situation where the note is simply silent on an issue and the mortgage clearly covers the issue. I find that there is irreconcilable conflict between the note and the mortgage, both executed on March 15, 2002, as to whether an acceleration necessarily results in the prepayment charge becoming due. The note unambiguously allows prepayment with no penalty. The mortgage perhaps, in a very ambiguous fashion, allows the prepayment penalty. The provisions of the note then govern. The bankruptcy court erroneously concluded that the language in the First Dakota mortgage (as ambiguous and poorly written as it is) would, in effect, trump the language in the promissory notes to the contrary.

[¶80] What would have happened in the foreclosure action had TSE not filed for bankruptcy? A complaint seeking to foreclose a mortgage is unquestionably an equitable action. *See First W. Bank, Sturgis v. Livestock Yards,* 466 NW2d 853, 856 (SD 1991), which case cites *Lounsberry v. Kelly,* 142 NW 180, on reh'g 143 NW 369 (SD 1913). "Foreclosure of a mortgage is an equitable action and a court in equity has the power and the right to grant full and complete legal and equitable relief." *American Fed. Sav. v. Mid-America Service,* 329 NW2d 124, 126 (SD 1983) (*citing cases*). This principle of law was endorsed again in *Alma Group, L.L.C. v. Weiss,* 2000 SD 108, 616 NW2d 96. The question is, in part: would a South Dakota court of equity require the mortgagor to pay a

prepayment penalty where the mortgagee has exercised the option to declare the entire balance due and payable at once? I believe the answer would be "no." It would certainly be "no" under the facts of the present case.

[¶81] I respectfully disagree with the attempt of the bankruptcy court to distinguish *American Savings & Loan Association v. Mid-America Service Corp.*, 329 NW2d 124 (SD 1983). I find and conclude that this case clearly states the public policy of the State of South Dakota, especially under the facts of the present case. This is despite the fact that the *American Savings* case is not "on all fours" with the present case. This is of no consequence since broad principles are stated in *American Savings*. In short, when the lender chooses to accelerate, there is no prepayment and a prepayment penalty may not be applied. The South Dakota Supreme Court relied, in part, on *Slevin Container Corp. v. Provident Federal Savings & Loan Assoc.*, 424 NE2d 939 (Ill.App.1981). "We believe that where the discretion to accelerate the maturity of the obligation is that of the obligee, the exercise of the election renders the payment made pursuant to the election one made after maturity and by definition not prepayment." *Slevin,* 424 NE2d at 941.

[¶82] The attempt to distinguish *American Savings* based on the fact that a due on sale clause was there involved must fail. As the South Dakota Supreme Court noted, *Slevin* did not involve a due on sale clause. *See* FN 4 which quotes from *Slevin* (424 NE2d

at 940-41) to the effect "that where acceleration of an obligation is the result of nonpayment by the obligor the election to so accelerate is binding and may not be revoked in order to charge and collect a prepayment penalty."

[¶83] The facts in the present case are "stronger" than in *American Savings* where the notes themselves contained the prepayment penalty language. The facts as to equities are even stronger in the present case. What the bankruptcy court did was to order the payment of all principal due, all interest due on the principal, the prepayment penalty, and interest on the prepayment penalty. This is in the nature of at least a double recovery and the South Dakota Supreme Court would not find such to be equitable. I also see nothing in the promissory notes authorizing interest to be collected on the prepayment penalty.

[¶84] I agree with the holding of the bankruptcy court that the claim for the prepayment penalty arose, if at all, when the notice of acceleration was given. It was pre-petition. The provision of the mortgage dealing with First Dakota having the right to declare the entire indebtedness immediately due and payable would include "any prepayment penalty which Grantor would be required to pay." In other words, it was then or never. I find that it was "never" but the claimed prepayment penalty was, by virtue of the language of the mortgage, linked to the notice of acceleration. There is no language anywhere possibly tying a prepayment penalty to anything other than

the acceleration. No prepayment penalty is even suggested by virtue of the debtor filing for bankruptcy, First Dakota presenting claims in the bankruptcy court, or upon a sale of the secured property. Thus, any possible recovery by First Dakota must stem from 11 U.S.C. § 502(b). It cannot stem from 11 U.S.C. § 506(b) and the bankruptcy court should be affirmed in that regard. In addition, any prepayment penalty, in the language of 11 U.S.C. § 506(b), is not "provided for under the agreement under which such claim arose." The claim, if any, would arise under the promissory notes and does not. No party has briefed or raised any possible issue as to the effect of all contracts requiring the application of South Dakota law and the effect, if any, that this would have on 11 U.S.C. § 506(b), assuming that any recovery could be made under that section. The cross appeal of First Dakota should be denied. What can and cannot be recovered under 11 U.S.C. § 506(b) is not relevant in this case.

[¶85] The bankruptcy court did not address the question of the definition of "prepayment." No definition of the word was contained in any of the documents. As I have discussed above, I believe the South Dakota Supreme Court has told us very clearly that paying under an acceleration by the lender is not as a matter of law a "prepayment." South Dakota is not alone in so holding. *In Matter of LHD Realty Corp.*, 726 F.2d 327, 330 (7th Cir. 1984), the court held that the lender lost its right to a prepayment premium by electing to accelerate the debt. "This is so because

acceleration, by definition, advances the maturity date of the debt, so that payment thereafter is not prepayment but instead is payment made after maturity." *Id.* In *Zwayer v. Ford Motor Credit Co.*, 665 NE2d 843 (Ill. App. 1 Dist. 1996), the court agreed with the holding in *Slevin*. Defendant had claimed that acceleration is a form of prepayment and the court rejected the argument, holding that payment pursuant to acceleration of the maturity date by the lender is, by definition, not a prepayment. *Id.* at 846. In *Garza v. Chicago Health Clubs, Inc.*, 347 F.Supp. 955, 962 (N.D. Ill. 1972), the court held that, for purposes of the Illinois Retail Installment Sales Act, "acceleration of the debt does not constitute 'prepayment' . . . because of the ordinary meaning of the word . . . " The payment of a debt after acceleration is not a prepayment and the creditor is therefore not entitled to recover any prepayment penalty provided for in the note. *See Texas Airfinance Corp. v. Lesikar*, 777 SW2d 559, 563 (Tex.App. Houston 14th Dis. 1989) and *George H. Nutman, Inc. v. Aetna Business Credit, Inc.*, 453 N.Y.S.2d 586, 587, 115 Misc.2d 168, 169 (1982).

[¶86] Given the ruling of the court, there is no need to reach the "free cash flow" arguments advanced by TSF. There is also no need to address the TSF arguments about the prepayment penalty being void under South Dakota law because of its nature as liquidated damages. Finally, there is no need to address the TSF argument that First Dakota, by accepting payment under 11 U.S.C. § 502(b) of all

principal, all interest, the prepayment penalty, and more than $80,000.00 in interest on the prepayment penalty, has waived any right to its cross appeal and its claim that the bankruptcy court should have awarded relief under 11 U.S.C. § 506(b). The parties argue about the question of reasonableness. This, of course, would be relevant only under 11 U.S.C. § 506(b) (except perhaps in connection with an equitable look at what would be permitted in the foreclosure action). I do note in passing the following South Dakota statute dealing with Savings and Loan Associations: "Any real estate loan may be prepaid in part or in full, at any time, and the association shall not charge for such privilege of anticipatory payment an amount greater than one and one-half percent of the amount of such anticipatory payment." SDCL 52-8-8.

[¶87] The bankruptcy court should be reversed as to the prepayment penalty liability of TSE.

APPEAL OF BANKRUPTCY COURT'S ACTION IN APPROVING SETTLEMENT BETWEEN TRUSTEE AND MURPHY INTERESTS

[¶88] Murphy Brothers ("Murphy") filed a proof of claim for $2,574,340.00 in this bankruptcy case The claim stemmed from a loan agreement and two promissory notes given by TSE, one for $2,100,000.00 and one for $380,000.00. White Rock Pipeline, LLC ("White Rock"), a South Dakota limited liability company, had constructed a pipeline to the TSE plant. Murphy had financed this activity. TSE owned

51% of White Rock and the others, namely Murphy, Walter Woods, and Randy Kramer owned 49% collectively.

[¶89] TSE was required by a federal regulatory agency to acquire 100% ownership of White Rock. Money from Murphy made this possible. TSE did acquire such ownership and defaulted on its monetary obligations to Murphy.

[¶90] In February of 2005, trustee paid Murphy, with court approval, $1,986,000.00. In August of 2005, Murphy filed an amended proof of claim. Trustee and Murphy thereafter reached a settlement and the trustee presented it to the bankruptcy judge, seeking approval. TSF filed objections. An evidentiary hearing was scheduled but was cancelled based upon the agreement of all concerned to submit the motion on written evidence. On January 22, 2007, the bankruptcy court approved the settlement, issued a "letter decision" and supporting Order, and overruled the objections of TSF. TSF appealed. TSF raises a large number of questions on appeal, without suggesting answers to any of them. It is clear also that the trustee did not withhold any information from TSF but attempted to answer all questions and provide all requested documents.

[¶91] Approval of a settlement by the bankruptcy court should not be set aside unless there is plain error or abuse of discretion. *In re New Concept Housing, Inc.*, 951 F.2d 932, 939 (8th Cir. 1991), *citing Florida Trailer & Equip. Co. v. Deal*, 284 F.2d 567,

571 (5th Cir. 1960). The bankruptcy court should not substitute its judgment for that of the trustee. *Martin v. Cox* (In re Martin), 212 B.R. 316, 319 (BAP 8th Cir. 1988), *citing* Fed.R.Bankr.P. 8013 and *First Nat'l Bank of Olathe Kansas v. Pontow,* 111 F.3d 604, 609 (8th Cir. 1997). There are four well known factors to be considered when looking at a proposed settlement. These include (1) the probability of success in the litigation, (2) the difficulties, if any, to be encountered in the matter of collection, (3) the complexity of the litigation involved, and the expense, inconvenience, and delay necessarily attending it, and (4) the paramount interest of creditors and a proper deference to their reasonable views in the premises. *PW Enterprises, Inc. v. Kaler* (In re Racing Services, Inc.), 332 B.R. 581, 586 (BAP 8th Cir. 2005) (*quoting Drexel Burnham Lambert, Inc. v. Flight Transportation Corp.* (In re Flight Transportation Corp. Securities Litigation), 730 F.2d 1128, 1135 (8th Cir. 1984) (*citing Drexel v. Loomis,* 35 F.2d 800, 806 (8th Cir. 1929))).

[¶92] It is clear that the bankruptcy judge carefully considered the four factors set forth above. The lower court carefully examined the loan agreement, promissory notes, security agreement, transfers of ownership documents, disbursement agreement, and the proposed settlement itself. All the agreements and documents when the financing arrangement was first "put together" were part of the same transaction. The arguments of TSF to the contrary frankly make no sense.

[¶93] It is clear that Murphy was entitled to be paid all principal and interest due under the promissory notes and that TSE was long in default. Such obligations were not executory or contingent. As to the basic ingredients, Murphy had the probability of success in any litigation. This is the first factor. As to the second factor, there was no difficulty in collecting. Murphy was an over-secured creditor. As to the third factor, this would be the "driving force" behind the settlement, just as it is in the vast majority of cases that are settled. It is obvious that expenses and delays involved in litigation would be important considerations. As to the fourth factor, no creditor other than TSF has objected. The paramount interests of the creditors have been fully considered.

[¶94] In examining a proposed settlement, the bankruptcy court need not conclusively determine claims and need not have all the information necessary to resolve any factual dispute; if the bankruptcy court set out to resolve any factual dispute, there would be no point to the settlement. *Martin,* 212 B.R. at 319. Likewise, there is no need for the court to find that the settlement is the best result that can be obtained. *Id.* The court need only canvass the issues to determine that the proposed settlement does not fall "below the lowest point of reasonableness." *Id.*

[¶95] Looking at the brief filed by TSF in this appeal (CIV 07-1003), it would appear that TSF used the appeal of the Murphy matter (and other appeals) to more than extensively brief the questions involving the recusal motion. This allows an "end run" on the

page limitations of briefs in the District of South Dakota. Taking multiple appeals of multiple issues would apparently allow this but I do not approve of the tactics.

[¶96] I reject again the contention of TSF that the bankruptcy judge should not have decided the "Murphy matter" and should have recused.

[¶97] TSF argues that the bankruptcy judge gave "boilerplate approval" to the Murphy-trustee settlement. I disagree with that claim. In reading the letter opinion, it is obvious that the judge gave very careful and detailed attention to the proposed settlement. He certainly considered also all claims and objections raised by TSF.

[¶98] The parties argue a great deal about the significance of two exhibits from the bankruptcy court. Exhibit four (to which TSF had no objection) would tell us that the trustee compromised the Murphy claim of $964,793.13 down to $850,000.00. Revised exhibit four (to which TSF objected) presents a $60,000.00 disparity and was a matter of legitimate concern for the bankruptcy court. The lower court found and concluded, however, that even with the disparity, the proposed settlement was not unreasonable. I am unable to find that the bankruptcy court abused its discretion or committed error. Certainly, the trustee could have possibly achieved a better settlement but that is not the test.

[¶99] But for the proposed settlement, Murphy could have claimed pre-petition and post-petition

attorney fees (the latter being pursuant to 11 U.S.C. § 506), prepayment penalties of $200,000.00 pursuant to the terms of the $2,100,000.00 promissory note, and additional interest from November 30, 2005. Litigation on questions of interest calculations, credits, validity of late charges, reasonable attorney fees, and prepayment penalties would have been complicated and protracted. Both the trustee and Murphy wished to avoid all of this. The settlement as approved by the bankruptcy court was clearly within the range of reason and was appropriate.

[¶100] All requests for oral argument should be rejected. This case has been argued and "briefed to death."

ORDER

[¶101] Now, therefore,

[¶102] IT IS ORDERED AND ADJUDGED, as follows:

1) All requests for oral argument are denied.

2) The order denying recusal is affirmed.

3) The order transferring case for purpose of ruling on motion for leave to take deposition is affirmed.

4) The order denying motion to take deposition (of the trustee) is affirmed.

5) The order denying motion to reconsider, set aside, alter and/or (sic) amend orders is affirmed.

6) The order striking motion to reconsider, set aside, alter and/or (sic) amend orders is affirmed.

7) The order setting deadlines is affirmed.

8) The order approving fees of the trustee's attorney is affirmed.

9) The order allowing the recovery by First Dakota National Bank of a prepayment penalty is reversed and this matter is remanded to the bankruptcy court to proceed pursuant to the order and opinion of this court as set forth above.

10) The cross appeal by First Dakota National Bank is denied.

11) The order approving the Murphy-Trustee settlement is affirmed.

[¶103] Dated this 17th day of May, 2007.

BY THE COURT:

/s/ Charles B. Kornmann
CHARLES B. KORNMANN
UNITED STATES
DISTRICT JUDGE

ATTEST:

JOSEPH HAAS, CLERK

BY: /s/ Barbara J. Paepke
DEPUTY

(SEAL)

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA

In re:	) Bankr. No. 03-10194
TRI-STATE ETHANOL COMPANY LLC	) Chapter 7
Debtor.	) ORDER DENYING TRI-STATE FINANCIAL, L.L.C.'S MOTION FOR RECUSAL

In recognition of and compliance with the *Decision* entered this day,

IT IS HEREBY ORDERED that the *Motion for Recusal* filed on June 29, 2006, by Tri-State Financial, L.L.C., is DENIED.

So ordered this 1st day of September, 2006.

BY THE COURT:

/s/ Irvin N. Hoyt
Irvin N. Hoyt
Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA

In re:	) Bankr. No. 03-10194
	) Chapter 7
TRI-STATE ETHANOL COMPANY LLC	)
	) DECISION RE:
Debtor.	) TRI-STATE FINANCIAL,
	) L.L.C.'S MOTION FOR
	) RECUSAL
	)

The matter before the Court is the *Motion for Recusal* filed by Tri-State Financial, L.L.C.; the joinders thereto filed by James G. Jandrain, Randall P. Kramer, and ICM, Inc.; and the objections thereto filed by First Dakota National Bank and Trustee John S. Lovald. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A). This *Decision* and accompanying *Order* shall constitute the Court's findings and conclusions under Fed.R.Bankr.P. 7052 and 9014(c). As set forth below, the motion will be denied.

I.

Tri-State Ethanol Company, L.L.C., owned an ethanol plant near Rosholt, South Dakota. The plant was the company's primary asset. When the plant was built, the general contractor was North Central Construction, Inc. ("North Central")[1]. The four original

[1] During the pendency of this case, North Central became known as American Prairie Construction Company.

investors in Debtor, and their approximate initial percentage of ownership, were Tri-State Corn Processors, a farmers co-operative, 26%; several investors from Omaha, Nebraska, known as "the Omaha group," 42%; Williams Bio-Energy, 16%; and North Central, 16%. The plant was in operation during 2002 but was shut down in November of that year for maintenance. At the time of the shutdown, the plant was running inefficiently and was faced with high propane costs. An explosion occurred at the plant on December 31, 2002, while it was shut down. During 2003, Debtor used insurance proceeds to repair the damage. The plant, however, did not resume ethanol production.

Tri-State Ethanol Company, L.L.C. ("Debtor"), filed a Chapter 11 petition in bankruptcy on May 23, 2003. In the early months of the case, several matters were addressed; some were contested:

FILING DATE	SUMMARY OF MATTER AND DISPOSITION
May 30, 2003	Oral motion for use of cash collateral made by Debtor. A telephonic hearing with parties in interest was held. Debtor's request for authority to use cash collateral of $24,000 to meet payroll and related expenses that day was approved.
June 5, 2003	*Emergency Motion Authorizing Secured Creditor to Pay Debtor's Casualty Insurance Premium* filed by First Dakota National Bank ("First Dakota"). No party appeared in opposition

to the motion, which was considered on shortened notice, and it was granted. No appeal was taken.[2] North Central filed an untimely response regarding the content of any order approving the motion.

June 12, 2003 *Motion for Authorization to (1) Enter Into Compromise and Settlement Agreement with National Farmers Union Property & Casualty Company on Business Interruption Policy and (2) Request for Expedited Ruling and Hearing* filed by Debtor. Debtor's attendant request for limited and shortened notice was denied by order entered June 12, 2003, for lack of cause shown. No appeal was taken. Objections to Debtor's *Motion for Authorization* were filed by Klein National Bank, Peoples State Bank, South Dakota Board of Economic Development, and First Dakota. Most of the objectors expressed concerns about the disposition of the settlement proceeds; there were limited objections regarding the settlement itself. At the hearing, the parties reported to the Court they

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[2] Throughout this decision, the Court indicates when appeals were not taken from more significant orders. Some of those orders may have been interlocutory in nature. However, any party seeking appellate review of such an interlocutory order could have sought leave to appeal under 28 U.S.C. § 158(a)(3) and Fed.R.Bankr.P. 8003.

agreed the settlement could be entered into, but any proceeds would be distributed only upon subsequent order. No appeal was taken.

June 12, 2003 *Emergency Motions Authorizing Secured Creditor to Extend Credit to Pay Debtor's Payroll and for Preliminary Rule 4001(c) Hearing* filed by First Dakota. No party appeared at the hearing in opposition to the motion, which was held on shortened notice, and the motion was granted. No appeal was taken.

June 25, 2003 *Motion for Use of Cash Collateral* filed by Debtor. Debtor also requested and received a preliminary hearing. Responses were filed by the South Dakota Board of Economic Development, First Dakota National Bank, Klein National Bank, Peoples State Bank, and Farmers Cooperative Elevator Company. At the preliminary hearing, Debtor was authorized to use $31,500.00: $6,500.00 to pay employees' health insurance, $20,000 for payroll and taxes, and $5,000 for electricity, which was in accord with the several responses. No appeal was taken.

July 8, 2003 *Motion to Compel Acceptance or Rejection of Lease and for Relief of Stay* filed by JCB Finance, L.L.C., regarding Debtor's lease of a skid steer loader and a forklift. Debtor

filed a response stating it intended to assume the leases as part of its Chapter 11 plan. The parties reported an agreement at the hearing. Debtor was directed to notice the agreement for objections. Debtor failed to timely notice the agreement for objections, so the matter was placed back on the calendar for September 22, 2003. At the continued hearing, Debtor was directed to notice the settlement for objections by September 24, 2003. Debtor filed a motion for approval of its assumption of the leases on September 24, 2003, and amended the motion on September 25, 2003. Debtor's amended motion was uncontested, but apparently no proposed order was submitted. The leases were eventually abandoned by order entered January 22, 2004, when Debtor defaulted.

July 11, 2003 *Motion Seeking Adequate Protection or, in the Alternative, Relief From the Automatic Stay* filed by First Insurance Funding Corporation, which financed funding for insurance premiums. Debtor and First Insurance Funding soon reached an agreement, which was approved without objection after notice. No appeal was taken.

Aug. 14, 2003 *Motion for Partial Relief From Automatic Stay* filed by Debtor so it could continue participation in a consolidated

state court litigation commenced pre-petition by North Central. An objection was filed by the South Dakota Board of Economic Development wherein it incorporated its response to a companion pleading in Adv. No. 03-1032 (discussed below). The Peoples State Bank, Klein National Bank, and the South Dakota Corn Utilization Council joined Economic Development's objection. Ronning Engineering Company, Inc., and Determan Brownie, Inc., joined the Corn Utilization Council's objection. First Dakota and North Central each objected on substantive and procedural grounds.

As a companion to its partial relief from stay motion, Defendant-Debtor filed in Adversary No. 03-1032 a *Motion for Voluntary Abstention under 28 USC § 1334(c)(1)*. Defendant South Dakota Board of Economic Development filed an objection saying the Bankruptcy Court was better suited to expeditiously resolve the matter. Defendants South Dakota Corn Council, Peoples State Bank, Klein National Bank, Ronning Engineering Company, Inc., and Determan Brownie, Inc., all joined Economic Development's objection. Plaintiff North Central and Defendant First Dakota also objected on substantive grounds.

The Court took both motions under advisement and addressed them in a decision entered November 14, 2003. The Court denied both motions and directed the parties to continue their litigation in Adversary No. 03-1032. No appeals were taken.

Sept. 17, 2003 *Motion to Compel Compliance* filed by the United States Trustee due to lack of F.D.I.C. insurance on certain of Debtor's deposits. Debtor objected, arguing an account "sweep" agreement complied with 11 U.S.C. § 345 and the "sweep" agreement was being noticed for objections, which motion is discussed below. First Dakota also filed a response along the same lines. At the hearing, arguments of counsel were received. The Court declined to make an exception to § 345 by allowing the sweep agreement. The parties submitted an agreed order that comported with the Court's conclusions. No appeal was taken.

Sept. 18, 2003 *Motion for Extension of the Exclusive Period to File a Disclosure Statement and Plan*, wherein Debtor requested an extension to December 31, 2003, to file a plan. Debtor reviewed what it had been doing since the petition was filed. It stated it had determined, "based on the damage done [to its ethanol plant] by the explosion [on December 31, 2002] and the production

history of the plant, that re-engineering and reconstruction would be needed in order to allow the plant to restart." It also stated David VanderGriend, President of ICM, Inc. ("ICM"), had "issued a report dated August 7, 2003, detailing the re-engineering and reconstruction [of the ethanol plant] needed along with cost estimates and his recommendations." Debtor further stated the next step was to "find the necessary infusion of capital to proceed with the VanderGriend recommendations. That required cooperation by First Dakota National Bank working with the Debtor[,] and a new funding source[,] Tri-State Financial, LLC." This statement appears to be one of the first formal acknowledgments of the existence of Tri-State Financial, L.L.C. ("Tri-State Financial"), in the case file. Debtor described Tri-State Financial in the motion as "a new limited liability company composed of investors who were willing to invest funds in the re-engineering and reconstruction of the Tri-State Ethanol plant to allow it to restart and to operate competitively in the marketplace. Some of the current interest holders in Tri-State Ethanol became investors in Tri-State Financial." No objections to this motion were filed, and Debtor's exclusivity period for filing a plan was extended to December 31, 2003.

On September 25, 2003, Debtor filed three motions. The first was an amended motion to assume leases on equipment, which was approved without objection, as discussed above. The second was a *Motion to Confirm and Establish Debtor in Possession Account at First Dakota National Bank*, in which Debtor sought court approval for an exception to § 345. The United States Trustee objected, saying the proposed account "sweep" did not comply with § 345. The United States Trustee also argued other banks in the region were capable of pledging securities under § 345(b)(2) and Debtor had not shown First Dakota was unable to pledge such securities or obtain a bond under § 345(b)(1). Both parties requested a continuance of the original hearing date. Evidence was received on October 22, 2003, and the parties were directed to submit an agreed order with which the United States Trustee was comfortable. The agreed order was submitted and entered. No appeal was taken.

Debtor's third motion filed on September 25, 2006, was the *Motion to: (1) Approve Stipulation and Agreement for Post-petition Financing, Use of Cash Collateral and Plan Treatment of First Dakota National Bank; (2) Incur Debt with Administrative Expense Priority over other Administrative Expenses (Super Priority); (3) Grant a Post-petition Lien on All of Tri-State Ethanol's Pre-petition Assets to Secure the Grant of an Administrative Expense Priority; and (4) Authorizing the Debtor to Contract for the Re-engineering and Reconstruction of the Plant* ("Motion

to Approve Re-engineering[3] Stipulation") and an accompanying *Stipulation and Agreement for Post-petition Financing, Use of Cash Collateral and Plan Treatment of First Dakota National Bank* ("Stipulation"). The Stipulation was composed of several provisions for funding a re-engineering of the ethanol plant. As summarized by the Court in a December 12, 2003, decision, these provisions included:

1. Debtor would contract with a company called ICM and a general contractor, which also might be ICM, to reconstruct the ethanol plant in the manner outlined in an August 7, 2003, report by David VanderGriend, the President of ICM. The August 7, 2003, report was defined as the "Startup Plan." The parties to the Stipulation estimated that interim overhead costs between September 2003 and January 2004 would be $270,530 and that startup costs, through the first 14 days of production, would be $467,500.

2. Debtor would contract with "an independent management firm . . . to direct the future operations" of the ethanol plant. The management that was hired would be acceptable to both Tri-State Financial and the Bank.

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[3] Various parties have used various terms to describe the post-petition work that was done at the ethanol plant to increase its production capacity and improve efficiency. The Court uses the term "re-engineering" herein to refer to that project.

3. Tri-State Financial and the Bank would approve all expenditures in advance and Tri-State Financial and the Bank would also approve in writing any expenditures incurred in addition to the "Budget," a term that was defined as Exhibits 1, 2, and 3 attached to the Stipulation. Exhibit 2 itemized a budget for the ethanol plant for September 2003 to January 2004. Exhibit 3 itemized three specific expenses and miscellaneous costs for the first fourteen days of production following the re-engineering and the reconstruction of the plant.

4. Tri-State Financial would loan Debtor not less than $2,000,000 to finance the "Startup Plan," interim costs, and startup costs. The $2,000,000 was to include "the funds that Tri-State Financial has already advanced to [Debtor] to finance [Debtor's] post-petition operating expenses." Debtor would not make any payments to Tri-State Financial or pay any interest on the loan until Debtor obtained confirmation of a plan. If the loan is not repaid by September 1, 2004, it will then bear interest at the prime rate (defined in the Stipulation) or 6%, whichever is less, with a repayment term of 20 years. Tri-State Financial would receive a superpriority lien under 11 U.S.C. § 364(d)(1) on all of Debtor's tangible, pre-petition assets, both real and personal.

5. After using the $2,000,000 in credit from Tri-State Financial, Debtor also would use $663,599.75 that is in its debtor-in-possession account (August 26, 2003, balance) at the Bank plus "any bio-energy or other government payment right, any further business interruption or other insurance settlement or litigation proceeds stemming from construction or design deficiencies or other pre-petition claims, and all other receipts of the Debtor which are the proceeds of pre-petition claims and all other receipts of the Debtor which are pre-petition rights" received by Debtor during the re-engineering and the reconstruction of the plant. These potential receipts were defined as the "Authorized Cash Collateral" that is secured to the Bank. The total Authorized Cash Collateral used was not to exceed $1,386,599.75. For the use of this cash collateral, the Bank would receive a superpriority lien under § 364(d)(1) on all of Debtor's tangible pre-petition assets, both real and personal). For Debtor's use of this cash collateral, the Bank would also receive under 11 U.S.C. §§ 361(a) and 363(a) a replacement lien effective on the petition date in all of Debtor's "rights in presently existing and after acquired tangible and intangible pre-petition and post-petition assets, the rents, issues, products, proceeds and profits thereof, including any causes of action or proceeds

arising out of or relating to the Debtor or its successor's assertion of any claims" under several Bankruptcy Code sections, corn and other inputs, bioenergy and other government benefits including any rights Debtor may have in tax credits, proceeds of lawsuits, insurance settlement or litigation proceeds and inventory and equipment. "This grant, however, provided there is no default, shall in no way limit the Debtor's right to transfer the Debtor's tax credits to equity holders of the Reorganized Debtor free from any such security interest, to be freely used by and available to such equity holders."

6. To the extent that both the Bank and Tri-State Financial have a superpriority lien on the same pre-petition assets, Tri-State Financial shall have first priority on the first $1,000,000 in assets, the Bank shall have a second priority for the cash collateral used up to $1,000,000, Tri-State Financial shall have third priority for "any additional cash collateral advanced" up to $1,500,000, and the Bank shall have fourth priority "in the amount of any additional funds advanced." If Tri-State Financial advances more than $2,500,000, it will be treated as an unsecured administrative claim under 11 U.S.C. § 364(c)(1).

7. Debtor agreed that it would bear "any shortfall in the funds needed for the Startup Plan, interim costs and startup

costs." Debtor stated that it now had the necessary funds or it would have them available when they were needed.

8. Phase II improvements as set forth in the Startup Plan, except the thermal oxidizer that may not be legally required, would be completed with financing through operating profits or additional capital. No distributions will be made to equity holders until Debtor, the Bank, and Tri-State Financial are satisfied that the Phase II improvements have been appropriately financed.

9. Debtor warranted that all issues with Alliance Pipeline Company have been resolved and that the plant will receive an uninterrupted supply of natural gas pursuant to a currently existing contract between Debtor and Alliance Pipeline Company.

10. The Bank holds a pre-petition a [sic] claim of $8,757,521.53 on the original construction note plus accruing interest and attorneys' fees and a second claim of $627,577.88 on an operating note plus accruing interest and attorneys' fees. The Bank is over secured. Debtor's original debt agreements with the Bank will remain in full force and effect and will be recognized and assumed in Debtor's plan. The Bank will continue to waive its right to assess a default rate of

interest so long as no default or breach of the Stipulation occurs.

11. Debtor will begin making payments to the Bank on March 1, 2004, or 30 days after the plant recommences production, whichever is earlier. These payments will be $117,700 per month on the original note and $10,500 per month on the operating note. "To the extent a reorganization plan has not yet been approved, these [payments] will be considered as adequate protection payments to [the Bank] and junior lieners whose equity position in the Debtor's assets is being eroded by the accrual of interest on Debtor's obligations to [the Bank]."

12. Debtor will file and serve its plan by January 1, 2004. Debtor must obtain confirmation of a plan by July 1, 2004, that has terms consistent with the Stipulation.

13. Upon confirmation of a plan proposed by Debtors [sic], Tri-State Financial's "position will be converted purely to equity and [the Bank] shall retain its position in the Pre-Petition Collateral and the Post-Petition Collateral provided for under [the Stipulation]." Further, the Stipulation provided that Rosholt Farmers Elevator and other producers who have unsecured claims for corn previously sold to Debtor will be "invited to contribute their claims dollar for dollar with

the capital contributed by [Tri-State] Financial equity holders and will become equity owners upon confirmation." When Tri-State Financial's lien position is converted to an equity position, Tri-State Financial agreed to disclose to the Bank "the identities of all equity owners of the Reorganized Debtor and the ownership interest of each." [Footnote omitted.]

14. If Debtor defaults on its monthly payments to the Bank under either the Stipulation or Debtor's confirmed plan, the Bank will be entitled, upon an affidavit of default, to its choice of relief from the automatic stay or conversion of Debtor's Chapter 11 case to a Chapter 7 case or dismissal of the Chapter 11 case.

15. Debtor will release and discharge the Bank and its participating lenders from all claims that Debtor or its assigns now has against the Bank or its participating lenders, specifically including any "lender liability" claims, for damages caused by or arising out of the loan transactions, loan servicing, or any negotiations concerning the sale of Debtor's assets or the assumption of the Bank's rights in the loans.

16. Before confirmation, Debtor will cure any delinquencies on any obligation secured by an interest superior to the Bank, including real estate taxes and TIF bond payments, but excluding North

Central's claim and any other unliquidated claim.

17. The Bank will not advance its state court cause of action (Civ. No. 03-91 in Roberts County, South Dakota) against guarantors Tri-State Corn Processors Cooperative, Randy Kramer, and James Jandrain so long as there is no default under the Stipulation. If a default occurs, these guarantors agree to execute confessions of judgment within ten days of a written demand by the Bank. The lawsuits will be dismissed upon confirmation of a plan.

18. Debtor will maintain casualty insurance that is acceptable to the Bank and Tri-State Financial on all personal property and real property improvements and the Bank and Tri-State Financial shall be named the loss payee and mortgagee.

19. Nothing other than the entry of an order approving the Stipulation was required to make the Bank's and Tri-State Financial's rights under the Stipulation "valid, enforceable, attach and perfected[.]"

In re Tri-State Ethanol Company LLC, Bankr. No. 03-10194, slip op. at 4-8 (Bankr. D.S.D. Dec. 12, 2003).

Objections to the Motion to Approve Re-engineering Stipulation were filed by the South Dakota Board of Economic Development, the South Dakota Corn Utilization Council, Interstates Electric

& Engineering Company, Inc. ("Interstates Electric"), North Central, and Gaylor Engineering. Debtor resolved the objections of the South Dakota Board of Economic Development and the South Dakota Corn Utilization Council. An evidentiary hearing was held October 22, 2003, to address the remaining objections. The Court received several exhibits and the testimony of David VanderGriend of ICM; William Taylor, the attorney who had been representing Debtor in the state court litigation surrounding the plant and its construction; James G. Jandrain and John Hoich, members of the Omaha Group and investors in Tri-State Financial; and Dan Swanda, a lending officer from First Dakota who handled complex loans. At the conclusion of the hearing, the Court requested proposed findings of fact and conclusions of law from each party.

On October 8, 2003, creditor Eugene Paulson[4] filed, while Debtor's Motion to Approve Re-engineering Stipulation was pending, a *Motion for Reduction of Debtor[']s Exclusivity Period to Original 120 Days*. Debtor and First Dakota each objected, and the South Dakota Corn Utilization Council joined First Dakota's objection. Following a hearing on October 22, 2003, the Court reserved a ruling until other pending matters were resolved, including Debtor's Motion to Approve Re-engineering Stipulation.

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[4] The motion contained signature lines for both Roger Hansen and Paulson, but only Paulson signed it.

The Court deemed Paulson's *Motion for Reduction* moot when Debtor's extended exclusivity period expired December 31, 2003.

On October 14, 2003, Debtor filed, also while Debtor's Motion to Approve Re-engineering Stipulation was pending, a *Motion for Use of Cash Collateral.* Debtor wanted permission to borrow $50,211.30 from Tri-State Financial and $25,105.65 from First Dakota to pay eight full-time employees and a property insurance premium. First Dakota filed a response and clarified it had consented to Debtor's use of $25,106.65 in cash collateral and the amount to be borrowed from Tri-State Financial was $25,106.65, not $55,106.65. The motion was approved in the amounts as clarified by First Dakota, and First Dakota was given a replacement lien. This was Debtor's only transaction with Tri-State Financial that was court-approved. The only other request for approval of an agreement with Tri-State Financial was the Motion to Approve Re-engineering Stipulation.

Debtor filed a second cash collateral motion on November 26, 2003, while its Motion to Approve Re-engineering Stipulation was still pending. Debtor sought use of First Dakota's cash collateral to pay a liability insurance premium. First Dakota filed a response stating it consented to Debtor's use of $40,000.00 and clarified Debtor was actually asking for retroactive relief since the Bank had already wired funds to prevent the insurance policy from being cancelled. North Central objected on the

grounds the motion did not contain all the information required by local rule and on the grounds it was also entitled to adequate protection. Upon the parties' agreed orders (preliminary and final), Debtor was authorized to use the $40,000.00, and First Dakota was given a replacement lien.

Two other pleadings were filed while the Court had under advisement Debtor's Motion to Approve Re-engineering Stipulation. On December 9, 2003, Zurich American Insurance Company filed a motion seeking payment of post-petition insurance premiums and a deadline for Debtor to assume or reject the contract of insurance. The motion was withdrawn before the scheduled hearing. The other was a motion filed by Eugene Paulson on December 10, 2003, in which he sought the appointment of a Chapter 11 trustee and an unsecured creditors committee. Paulson argued unsecured creditors holding smaller claims were not being appropriately recognized and Debtor was losing about $7,000.00 per day because the ethanol plant was still shut down. Debtor filed an objection stating it had been "consistently attempting to obtain the necessary funding to reconstruct the Ethanol plant and ha[d] worked to protect the interest of all involved[.]" The United States Trustee responded, stating he would fulfill any order of the Court to appoint a committee. He also stated an appointment of a trustee would take some time since the person appointed would have to have a background check and be bonded. The United States Trustee opined operation of the plant would more

properly be the result of a confirmed plan. Five creditors also objected to Paulson's motion on various grounds. The Court directed the United States Trustee to again attempt the appointment of an unsecured creditors committee but denied Paulson's request for a Chapter 11 trustee for lack of cause. No appeal was taken. However, the United States Trustee later reported he was unable to constitute a committee.

On December 12, 2003, the Court entered its Decision on Debtor's Motion to Approve Re-engineering Stipulation. Therein, the Court reviewed applicable law and concluded:

> The Stipulation proposed by Debtor cannot be approved for three primary reasons. First, the Stipulation's wide-sweeping provisions are more akin to the basis for a plan of reorganization and should not be approved absent the full disclosure, notice, and balloting provisions that are provided by the confirmation process. As noted in *BankWest v. Todd*, 49 B.R. at 636-37, a large-scale cash collateral agreement is not appropriate until a plan is on the table. The Stipulation proposed by Debtors [sic] and the consenting lenders does more than provide operating funds until a plan is confirmed. It not only proposes substantial alterations to Debtor's ethanol plant and the incurrence of substantial debt, it also proposes to change the position of present equity holders. That should only be done through the confirmation process.

Second, Debtor failed to show that the necessary credit and use of cash collateral could only be obtained through a superpriority lien. Of the three components necessary for allowing a superpriority lien – that the financing deal is an exercise of sound and reasonable business judgment, that alternative financing is not available, and that the proposed financing is in the best interests of the bankruptcy estate and creditors – none were met. See *Swedeland*, 16 F.3d at 564, and *Phase-I*, 285 B.R. at 495-96.

While there was some evidence that the Stipulation was the product of a reasonable business judgment, it was tainted by the fact that Debtor primarily dealt with insiders. Moreover, the Stipulation provided that some insiders' equity positions could be improved and some insiders' personal guarantees of Debtor's operating note would be put on hold.

There was no evidence that Debtor could not obtain alternative financing, such as offering a security interest in unencumbered assets. According to Debtor's own schedules, its assets exceed its liabilities by over $7,000,000. Debtor offered no supporting documentation when Jandrain tried to dispute that number at the hearing. Further, the record was weak regarding what other prospective lenders were contacted, what terms they were offered, and why they refused to deal with Debtor.

As to whether the proposed financing was in the best interest of the bankruptcy estate and creditors, the record was essentially nonexistent. What the effect that the financing deal would have on other creditors was simply unknown. As noted in *Seth Co.*, 281 B.R. at 153, a superpriority lien is an extraordinary remedy. It should be given only when the proponents have clearly met all the requirements of § 364(d). That was not accomplished in this case.

Finally, Debtor's Motion to Approve [Multi-faceted Stipulation] and the attendant Stipulation will not be approved because Debtor failed to show that existing creditors are adequately protected. *See Swedeland*, 16 F.3d at 564, and *Mosello*, 195 B.R. at 292. To demonstrate adequate protection, Debtor needed to present good appraisals and valuations that permitted the Court to compare the current value of the plant to its projected value following the re-engineering and reconstruction. The only current valuation the Court had was the value that Debtor had put in its schedules, and Debtor's insiders took exception to that value at the hearing. The only projected value of the plant following the re-engineering and reconstruction was $24.2 million as stated in testimony by Jandrain and Swanda, but there was little documentation to support that number. The Court also needed to know Debtor's current equity position, if any, based on the present position of its several secured creditors, and it needed to

> know how these secured creditors' positions would be affected by the re-engineering and reconstruction and by the superpriority liens that Debtor wanted to give. Without those numbers, the Court could not determine if existing secured creditors' claims needed protection from erosion and, if so, to what extent.

In re Tri-State Ethanol Company LLC, Bankr. No. 03-10194, slip op. at 27-30 (Bankr. D.S.D. Dec. 12, 2003). No appeal was taken.

William L. Biggs, Debtor's out of state counsel, filed a fee application on December 29, 2003. Responses filed by the United States Trustee and North Central in mid January 2004 disclosed a possible conflict of interest between Biggs' firm's representation of both Debtor and some equity security holders who had formed Tri-State Financial. The Court took the fee application under advisement and directed the United States Trustee to investigate further Biggs' law firm's possible conflict of interest. The United States Trustee's investigation resulted in a motion to vacate the order approving the employment of Biggs' law firm. Biggs and his firm responded by withdrawing as counsel and declaring they would not seek any fees from Debtor or the bankruptcy estate. The withdrawal was approved by order entered February 27, 2004. No appeal was taken.

Debtor filed a plan and disclosure statement on December 31, 2003. At a hearing on February 10, 2004, Debtor was directed to make changes to the

disclosure statement to resolve the objections filed by North Central. Debtor filed the amended disclosure statement and another plan on February 17, 2004. Debtor's plan was set for a confirmation hearing on April 7, 2004. Debtor filed another modified plan on March 2, 2004, and it was set for a confirmation hearing on April 7, 2004.

On January 21, 2004, Debtor sought approval to finance $117,126.00 in various insurance premiums. No objections to the motion were filed, and the motion was granted. Debtor filed a similar motion on April 9, 2004, to finance its property insurance premiums. That motion, too, was approved, with some clarifications in the order to address concerns raised by First Dakota.

Eugene Paulson filed a second motion for appointment of a Chapter 11 trustee on February 12, 2004. Objections were again filed by various creditors, and an evidentiary hearing was set for April 7, 2004.

Eugene Paulson and Roger Hansen filed a plan and disclosure statement on February 23, 2004. A hearing on their disclosure statement was also set for April 7, 2004.

By motion filed February 27, 2004, Debtor sought another extension of its exclusivity period to obtain confirmation of a plan. Tri State Corn Processors Cooperative joined. The motion was denied because it

had not been filed before the first extended exclusivity period expired, as required by 11 U.S.C. § 1121(d). No appeal was taken.

Tri-State Financial first formally appeared in the case on March 8, 2004, when Attorney Biggs, Debtor's former counsel, filed a notice of appearance on the entity's behalf.

During this first year of the case, two adversary proceedings were commenced. Debtor, Tri State Corn Processors Cooperative, and Traverse Guarantors commenced Adversary No. 03-1053 against Traverse Electric Cooperative, Inc., on October 31, 2003. They alleged Traverse Electric Cooperative violated the automatic stay when it collected on a letter of credit. Tri State Corn Processors Cooperative and Traverse Guarantors were dismissed as plaintiffs on January 8, 2004, for lack of standing. The adversary proceeding itself was dismissed on March 3, 2004, when the parties failed to comply with a scheduling order.

North Central commenced Adversary No. 03-1032 against Debtor and several other parties involved in the ethanol plant construction. North Central sought a determination of the validity, priority, and extent of the liens and other encumbrances on Debtor's assets. This adversary proceeding was, in significant measure, a continuation of the state court action that had been pending when Debtor filed for bankruptcy relief. Counter and cross-claims followed. Defendant First Dakota sought partial summary judgment in late 2003. The issue presented was the

impact of certain lien waivers. Plaintiff North Central filed a cross motion in mid-January 2004. Responses and briefs were received. Some contested discovery issues arose in the interim.

As a consequence of the partial summary judgment motions in Adversary No. 03-1032 and the effect the ruling might have on confirmation of a plan, by order entered March 24, 2004, the Court cancelled the April 7, 2004, hearings on Hansen and Paulson's disclosure statement and second motion for appointment of a Chapter 11 trustee and on confirmation of Debtor's March 2, 2004, plan. While the partial summary judgment motions were pending, the Court continued to receive ballots on Debtor's plan and responses to Paulson and Hansen's disclosure statement and second motion for appointment of a trustee. In the interim, Debtor sought and obtained approval of another insurance premium financing agreement. Debtor also sought approval of settlements with the South Dakota Board of Economic Development and the South Dakota Corn Utilization regarding plan treatment.

On May 10, 2004, the Court entered its decision on the cross-motions for partial summary judgment in Adversary No. 03-1032. First Dakota's motion was denied, and North Central's motion was granted in part. First Dakota appealed the decision. The United States District Court for the District of South Dakota dismissed the interlocutory appeal *sua sponte* for procedural miscues.

On May 10, 2004, the Court scheduled a status conference for May 25, 2004, on the pending matters in the main case. At the status conference, Hansen and Paulson's disclosure statement and second motion for appointment of a Chapter 11 trustee and Debtor's modified plan were reset for an evidentiary hearing on June 21-22, 2004. Debtor's pending settlement motions with the South Dakota Board of Economic Development and the South Dakota Corn Utilization were set to be heard with the evidentiary confirmation hearing on June 21-22, 2004.

On May 26, 2004, creditors William F. Murphy Self Declaration of Trust and Mike D. Murphy ("Murphy Trust") filed their own plan and disclosure statement. The hearing on their disclosure statement was set for June 21-22, 2004, with the several other matters.

On May 26, 2004, the United States Trustee filed a *Motion to Dismiss or Convert to Chapter 7* on the grounds Debtor was behind on quarterly fee payments and there was an inability to confirm a plan. The United States further stated,

> Once the Court determines that cause exists to dismiss or convert this case, it should consider the best interests of creditors and the estate before deciding whether to dismiss or convert the case. *In re Mazzocone*, 180 B.R. 782, 785 (E.D. Pa. 1995). The Debtor has significant assets which, if properly marketed, could generate sufficient cash to pay secured claims and at least a portion of the

> unsecured claims. United States Trustee believes that it is in the best interests of the creditors in this case that it be converted to a chapter 7 proceeding.

Many objections to this motion were filed, including approximately 85 form-type objections by corn producers who were owed money for corn they had delivered to Debtor's ethanol plant. The form objections stated:

> I, [name or names inserted] have a claim for corn delivered to Tri State Ethanol LLC and/or a claim for the guarantors paid Travers Electric cooperative. I object to dismissal or conversion to Chapter 7 of this bankruptcy. I support the debtor's reorganization plan, as this plant is very much needed in the community and should be given a working chance to recover.

A signature followed.

In its objection to the United States Trustee's motion to dismiss or convert, Debtor addressed only the quarterly fees. It said the check initially had been mailed to the wrong address and the error had now been corrected. The Murphy Trust responded and urged the Court to consider its liquidation plan before ruling on the United States Trustee's motion. In an objection filed June 8, 2004, the Tri State Corn Processors Cooperative stated:

> Progress on the improvements to the Debtor's facility is good and it is anticipated the facility will be operational soon. The

> proposed Plan by the Debtor is in the best interest of Tri State Corn Processors Cooperative, whose membership consists of local individuals including many farmers. Conversion or dismissal at this time would damage those individuals.

This was the first indication the Court found in the record that re-engineering work on Debtor's ethanol plant had continued, even though Debtor had failed to obtain court approval for that work. The South Dakota Board of Economic Development made a similar comment in its June 11, 2004, objection. First Dakota's objection filed on June 17, 2004, elaborated:

> The Debtor has various owners who have been funding its employee, insurance and other overhead costs, as well as the necessary reconstruction and re-engineering of the Debtor's plant. First Dakota believes that if the case converted to Chapter 7, there is very substantial risk that Tri-State Financial, LLC, will no longer fund the reconstruction and start-up and operation of the plant, and the value of the plant would be reduced to liquidation value. First Dakota is informed that if the case is dismissed, the owners of the Debtor will complete the construction process and fund the start-up process which should result in generation of sufficient revenues to pay all creditors in full, preserve the positions of employees and save the equity positions of the corn producers and other owners of the plant.

Ronning Engineering responded saying it preferred conversion over dismissal since a return to the state court litigation – if the case were dismissed – would be expensive and detrimental to it.

On June 18, 2004, Paulson and Hansen filed a pleading that essentially said they were withdrawing their proposed plan and disclosure statement if a Chapter 11 trustee were not appointed. Therein, they too referenced the reconstruction and re-engineering that apparently was continuing on the ethanol plant:

> [The South Dakota Board of Economic Development] claim[s] that they support the Debtor[']s plan because they believe, for whatever reason, that their plan will somehow repay the creditors. Yet they know nothing about whether the Debtor has the funds necessary to implement their plan. They seem to know nothing about the millions of dollars that are being expended on the plant now and for the last several months. . . .
>
> . . . .
>
> We believe from information and belief that the Yankton Bank [First Dakota] has pretty much called the management shots on this business frm [sic] the first. We also believe that they are pretty much responsible for it being in the shape it is in at this point. We believe, from the information that we have been able to obtain, that they may be paying for the supposed improvement that are going on now. . . .

Motion for Permission to Withdraw Disclosure . . . , pp. 1-2, by Eugene Paulson and Roger Hansen (June 18, 2004) (file doc. 676). Hansen and Paulson went on to argue against some of the reconstruction and re-engineering proposals made by ICM.

Jerrold L. Strasheim, out of state counsel for Tri-State Financial, L.L.C., made his first appearance in the case on June 18, 2004, when he sought and obtained admission *pro hac vice* through local counsel Terry N. Prendergast.

A hearing on the several pending matters was held June 21, 2004. Debtor withdrew its modified plan, and a July 28, 2004, hearing was set for confirmation of another modified plan Debtor intended to file. The hearings on Hansen and Paulson's disclosure statement, the United States Trustee's motion to dismiss or convert, Hansen and Paulson's second motion for appointment of a Chapter 11 trustee, and Murphy Trust's disclosure statement were continued to July 28, 2004. Debtor's proposed settlements with the South Dakota Board of Economic Development and the South Dakota Corn Utilization Council were approved.

During the June 21, 2004, hearing, Debtor, North Central, Interstates Electric, Tri-State Financial, and John Hoich reported an agreement on the record that would be noticed for objections. The report was initially given by Ronald J. Hall, counsel for North Central.

Your Honor, this is an agreement for resolution of North Central's claim as well as or – and objections as well as Interstates Electric's objections and claims. And the agreement is both with the debtor and with Tri-State Financial, LLC, as well as John Hoich [sic] wh – it's my understanding – has personally committed to this deal. And the deal is as follows:

North Central has agreed to sell and Tri-State Financial, LLC/John Hoich [sic] as a buyer have agreed to purchase North Central's claim in Class 12 and North Central's equity interest in Class 18 of the debtor's plan for a purchase price of two point five million ($2,500,000), which will be payable in full upon North Central's delivery of an appropriate document transfer and assignment of its claim and interest to the buyer, and that transfer will be without recourse.

Second, this purchase does include the purchase and transfer of Interstates Electric's Class 13 claim for the price of four hundred seventy-five thousand dollars ($475,000) cash payable in full out of the total purchase proceeds upon Interstates Electric delivering appropriate transfer document. And again that – [the Court interrupted to clarify the amount] Again that, that transfer by Interstates Electrics will receive the balance of its claim in Class 13 in the amount of thirty-four thousand seven hundred eighty-three dollars $34,783) under the plan as modified,

> and that will be over three years at nine percent.
>
> Third, the purchaser and – or the parties agree that that total purchase price of two point five million will be allocated as follows: For North Central, North Central's Class 12 claim, one point five million, for North Central's Class 18 interest – equity interest, one million; and obviously four hundred and seventy-five thousand dollars ($475,000) of that amount, of the one point five in class – in North Central's Class 12, four hundred seventy-five thousand dollars ($475,000) of that is to be allocated to Interstates Electric's Class 13 claim.

TRANSCRIPT OF RECORD at 8-9, *In re Tri-State Ethanol Company LLC*, Bankr. No. 03-10194 (June 21, 2004) (file doc. 974).

Debtor's group health insurance provider, Wellmark Blue Cross and Blue Shield of South Dakota, sought relief from the stay on June 7, 2004, to cancel the policy due to a default on premium payments. Though Debtor did not resist, the Court was made aware the parties were working on an agreed order.

Debtor filed its modified plan on June 25, 2004, and a confirmation hearing was set for July 28, 2004. While this modified plan was pending, on July 2, 2004, Debtor filed another motion to incur secured debt. Therein, Debtor stated:

> Debtor is in the business of providing ethanol to various customers and is in the

> process of rehabilitating its plant so that it may continue to provide such ethanol and in the process thereof, needs the sum of $160,000.00 for the months of July and August in order that wages can be paid and expenses paid as shown above.

The source of the funds was to be First Dakota. Debtor requested preliminary authority for $35,000 by July 9, 2004, for wages and attendant insurance and taxes, "and equipment and utility payments shortly after such date." The motion went on to state Debtor contemplated it would be "up and running in the middle of August and the Plan will be confirmed prior to the end of August." First Dakota filed a response saying it had agreed to allow Debtor to use collateral in the amount stated but not to loan Debtor additional funds; the South Dakota Board of Economic Development and the South Dakota Corn Utilization Council joined First Dakota's response. North Central filed a response setting forth concerns about the lien to be given to First Dakota and whether it (North Central) would remain adequately protected. At the preliminary hearing on July 9, 2004, Debtor was authorized to use $10,401.49 for payroll.

On July 14, 2004, North Central filed a *Motion to Approve Compromise Settlement and Release* regarding the deal among North Central, Debtor, Tri-State Financial, and Interstates Electric Engineering Company, Inc., as had been referenced on the record June 21, 2004. Tri-State Financial filed a response stating the "orally announced stipulation does not

include all terms of the settlement and in some aspects is unclear or incomplete, or both. . . . " It went on to state the parties were still negotiating. Debtor filed a response and stated, "[T]he Motion does accurately reflect the Agreement made by Debtor in Court but . . . Debtor is in a position in which it would be quite difficult for Debtor to enter into the proposed Agreement unless North Central Construction and Tri-State Financial are able to reach an Agreement." An evidentiary hearing on North Central's motion was set for July 28, 2004, with the several other matters. The Court later amended the scheduling order to move this matter to the afternoon of July 27, 2004, since it apparently would affect confirmation of Debtor's proposed plan on July 28, 2004.

Hansen and Paulson filed another plan and disclosure statement on July 23, 2004, thus rendering their earlier ones moot. The earlier ones were taken off the July 28, 2004, calendar.

On July 27, 2004, the Court first met with counsel in Chambers, and then counsel negotiated privately. On the record, the Court reported North Central's motion to approve its agreement with Debtor, Interstates Electric, and Tri-State Financial apparently was moot because the parties now disputed whether they had a deal on June 21, 2004. The Court also stated it could not force Tri-State Financial to consummate a deal. The Court accordingly advised the parties the confirmation hearing set for the next day would be a contested matter and confirmation appeared "difficult to obtain" based on the

in-chambers discussion. The Court advised the parties it would take up the United States Trustee's motion to dismiss or convert as the second matter of the day if Debtor did not obtain confirmation of its modified plan.

On July 28, 2004, the Court took appearances and called the hearing on the confirmation of Debtor's second modified plan dated June 24, 2004. Debtor's counsel, A. Thomas Pokela, advised the Court Debtor was joining the United States Trustee's motion to dismiss. In response, the Court stated, "I guess what I am interested in is whether it would be appropriate to dismiss or convert, and that under the Code is in – I think in the best interest of the creditors."

Attorney Pokela acknowledged the Court's statement and asked whether the Court wanted a witness or argument on that issue. The Court left that decision to Attorney Pokela. Attorney Pokela then presented as a witness David VanderGriend, the owner and president of ICM. VanderGriend testified, on direct and cross-examination, ICM had been working, without a contract, for six months to re-engineer Debtor's ethanol plant to increase its production capacity to 20 million gallons per year. He said ICM had expended $1.2 million to date and "Mr. Hoich and his group" had put an additional $900,000 into the re-engineering project. VanderGriend stated ICM expected to be paid for its work but it had agreed to take an equity position in the plant in exchange.

VanderGriend testified the plant, after completion of additional work at a cost of over $200,000, would be operational September 1, 2004, would be licensed by the state by September 15, 2004, and, once operating, would produce at 20 million gallons about two weeks later and at 22 million gallons six months later. VanderGriend testified the plant should cash flow within 90 days after start-up. VanderGriend opined the plant would generate sufficient revenues to allow Debtor to pay all its creditors in full over time. He estimated creditors' claims would total $5 million. He did not know how much it would cost Debtor to resolve pending construction-related litigation. He did not know whether some natural gas pipeline issues had been resolved.

VanderGriend stated a subsidiary of ICM, United Bio Energy, was expected to be hired by Debtor to operate the plant. He testified Debtor's staff had doubled from the original six to twelve, the twelve would constitute permanent staff, and another 20 permanent employees would eventually be added to make the plant the largest employer in Rosholt, South Dakota.

Regarding the value of the plant, VanderGriend testified it was currently worth about $25 million and would be worth 50% more as an operable facility. These values generated additional questions and clarifications during the remainder of the hearing.

The Court questioned VanderGriend about the value of the claims against Debtor. VanderGriend

again stated he thought the claims totaled about $5 million. The Court directed the witness to a liquidation analysis that indicated secured and unsecured claims totaled just over $19 million. In response, VanderGriend acknowledged he had no idea what kind of payments would be required to pay creditors. VanderGriend further testified operating funds that would be needed would be about $2 million per year.

James Jandrain, who holds an ownership interest in Debtor, next testified on Debtor's behalf. He is a Certified Public Accountant and holds a law degree but is not a licensed attorney. Jandrain acknowledged "all the members of the Co-op" and Randy Kramer had given personal guarantees "on a temporary operating loan" related to the ethanol plant before the plant filed bankruptcy.

Jandrain acknowledged claims against Debtor totaled just over $19 million. He reviewed an exhibit forecasting Debtor's income and expenses and acknowledged it did not include costs associated with pending litigation. He testified the plant would need an additional $3.5 million to become operational. Jandrain also testified Debtor already had spent for operating costs around $800,000 it had received as a government subsidy payment. Jandrain acknowledged present equity holders' interests would be diluted due to the need for additional capital. Finally, Jandrain acknowledged if the case were dismissed there was no binding agreement with creditors regarding how and when they would be paid and

Debtor had no plan to resolve the present state court litigation.

Debtor also called Steven Heesch, a Rosholt area farmer who was the chairman of Debtor's board of directors and who was also on the board of directors for Tri State Corn Processors Cooperative. Heesch testified the government subsidy payment was still being held by Debtor and had not been expended. Heesch testified he had been contacted by about nine potential buyers for the plant, including a couple just recently. He further stated an agent of another potential buyer had toured the plant since the bankruptcy began. Heesch testified the ethanol plant, after the explosion, had been completely repaired before Debtor filed bankruptcy but had not been "started up." Heesch said the bankruptcy filing was precipitated by a sale that fell through and First Dakota's impending foreclosure action. He acknowledged Debtor would again face the foreclosure action if the case were dismissed.

The Court received closing arguments from counsel. The United States Trustee, the Murphy Trust, North Central, Interstates Electric, and Ronning Engineering all argued in favor of conversion. First Dakota, Tri State Corn Processors Cooperative, and Debtor argued in favor of dismissal. The Court briefly noted problems with Debtor's plan and questioned whether this case had been filed in good faith and whether it was continuing in good faith. The Court ordered the case to be converted to Chapter 7 on oral findings and conclusions:

The most important advantage to conversion is that the Chapter 7 Trustee is independent, does not have a vested interest in who gets paid, when and how much. It would appear that the Chapter 7 Trustee may be able to get the plan[t] up and running within a relatively short period of time or offer the plan[t] for sale, also within a relatively short period of time. They may be able to [employ] ICM if that's appropriate and move for credit to complete the upgrade project, again if that's appropriate. They can also quickly assess independently whether dismissal is appropriate.

A dismissal, as has been pointed out in argument by counsel, puts everybody back to start. It puts them back into the place unknown as far as we're concerned.

Today we have a plan to get the plant back on track, and also we've got litigation that looms. The only evidence we have today is the plant's total worth was – I think the testimony was twenty-five million. Unsecured and secured debt is somewhere and estimated, I would say administrative costs would be somewhere in the range of twenty million. So for a sale, if that were to be effectuated, it would appear that everybody would be paid in full.

And for these reason [sic] I think that the case will be converted to a Chapter 7. As a caveat I would say that the debtor's principals and the debtor's counsel and other

> parties in interest I'm sure are aware, but I would caution them, that they would have to fully cooperate with the Chapter 7 Trustee to protect all of the debtor's assets from this moment forward and help him or her in the process of them doing their job the most quickly and efficient way.

TRANSCRIPT OF RECORD at 91-92, *In re Tri-State Ethanol Company LLC*, Bankr. No. 03-10194 (July 28, 2004) (file doc. 1322) (bracketed notes correct transcriptionist errors). The conversion order was entered July 29, 2004. No appeal was taken. The United States Trustee appointed John S. Lovald as the Chapter 7 trustee.

By motion filed August 3, 2004, Trustee Lovald promptly sought authority to complete the re-engineering of the plant and to operate it for three months. He proposed to use an account balance of $546,221.53, which was First Dakota's cash collateral, and a line of credit of $4,000,000 from a new business entity called "New Corp." A budget attached to the trustee's motion indicated $1.5 million of the total funds requested would be needed to complete the re-engineering project. Trustee Lovald sought preliminary authority to use $33,927.90 in cash collateral within the week to pay insurance premiums and another $64,654.00 for the coming payroll. The South Dakota Board of Economic Development filed a response to clarify the $1.5 million Trustee Lovald sought to finish the re-engineering of the plant did

not include any pre-conversion debt. A preliminary order was entered August 5, 2006, to allow the trustee's use of $33,927.90 in cash collateral to pay insurance premiums.

North Central filed an objection to the trustee's proposed expenditure of $1.5 million to complete the re-engineering and to the request for credit authority of $4 million. First Dakota filed an objection similar to North Central's. Interstates Electric also joined North Central's objections. It further stated it was confused by the significant increase in projected costs to complete the project from those presented by Debtor's witnesses at the July 28, 2004, hearing. Interstates Electric also argued grounds for giving the proposed creditors a super priority lien status were not shown and no showing had been made that completion of the re-engineering was appropriate when an attempted start-up of the plant might reveal latent problems that would actually decrease the value of the plant.

Trustee Lovald filed a supplement to his motion to list those persons or entities that had agreed to invest in New Corp. and the amounts each had pledged. Radio Engineering Industries, Inc., was to be the largest investor in New Corp. at $2,260,000 pledged; ICM was to be the second largest at $872,000. Tri-State Financial was not listed.

A preliminary hearing on the contested amount of Trustee Lovald's preliminary request was held August 6, 2004. The hearing minutes provided:

> Trustee Lovald was authorized to use preliminary cash collateral of approximately $70,000 to meet today's payroll, employ a consulting engineer, pay a necessary state permit fee, and other immediate related expenses. After receipt of the report from the estate's engineer, Trustee Lovald may authorize ICM to resume construction pending a final credit and cash collateral hearing on August 17, 2004, at 2:00 p.m. in Sioux Falls. ICM shall receive a priority lien for the reasonable and necessary costs for this interim construction. The last date for objections to Trustee Lovald's final request for use of cash collateral and to incur secured debt shall be moved back from August 23, 2004, to August 16, 2004, at 4:00 p.m.

Upon Trustee Lovald's request, the final hearing was rescheduled to August 25, 2004. The trustee's request was based upon several purchase offers he had received for the ethanol plant in its present state. On August 24, 2004, Trustee Lovald filed a second motion to reschedule. This time he said he had a purchase offer from ABUS, L.L.C., to purchase the plant. The hearing was rescheduled to September 2, 2004.

Upon the trustee's request at the September 2, 2004, hearing, most of the relief requested in his cash collateral and credit motion was deferred. The Court approved a limited use of $186,703.60 in cash collateral from Debtor's former debtor-in-possession account. First Dakota was also permitted to apply the balance of the bankruptcy estate's checking account,

about $253,296.40, as adequate protection payments for August and September 2004 (partial) and a "loan" payment. First Dakota's interest rate during "these periods" was not to exceed 9%. No further hearings were held on the deferred portions of the motion, and Trustee Lovald withdrew it on March 11, 2005.

On August 25, 2004, Trustee Lovald filed a motion for an extension of time in which the estate had to assume or reject any [unnamed] executory contracts since a potential purchaser of the plant might not want to continue some of them. Aux Sable Liquid Products, L.P., ("Aux Sable") objected. It apparently held one of the executory contracts the Chapter 11 debtor-in-possession had assumed. Aux Sable argued against the delay since it would only increase its administrative claim "with little hope of payment due to the replacement liens and the 'pending approval' [of a] Super Priority Lien of First Dakota National Bank." At the hearing, the parties agreed to an extension through November 30, 2004.

By motion filed September 10, 2004, Trustee Lovald sought approval of the terms regarding a sale by auction of the estate's assets, in essence the ethanol plant. Two potential buyers, Aux Sable and EXL Group, L.L.C. ("EXL") objected. At the conclusion of the hearing, the objections were overruled in part and sustained in part, and the sale terms and bidding procedures were set forth in the minutes and an order. The auction was set for October 22, 2004.

On September 23, 2004, Trustee Lovald filed a follow-up sale motion that included the sale terms and bidding procedures previously established by order and that identified EXL as the proposed initial buyer whose bid would be subject to upset at the October 22, 2004, in-court auction. EXL's offer was $18,800,000 and the assumption of a $1,500,000 construction debt to VanderGriend Construction and ICM that was incurred post-conversion. Approximately 81 form objections were filed that identified the objector and the amount of their claim and stated the plant should not be sold to EXL because it had no ties to the Rosholt area. The form objection further stated a sale

> to a consortium of Tri-State Financial LLC or its members and unsecured creditors who are willing to waive their claims against the bankruptcy and take an equity interest in the new entity formed by the consortium. Under the consortium approach, the Rosholt community and its businesses would undoubtedly benefit more than with a sale to EXL. More importantly, Claimant expects a better return on the equity that Claimant will obtain for waiver of its claim. . . . The approach of the consortium will come closer to paying Claimant, and other Claimants waving their unsecured claims, in full. Claimant does not see how this can hurt other creditors.

One of the objectors using the form pleading was James Jandrain, who said he held an unsecured

claim for $31,512.50. Tri-State Financial objected to this sale motion on the grounds the sale price to EXL was too low and the sale terms "unjustly" did not provide for payment of post-petition, pre-conversion re-engineering costs. Tri-State Financial briefly outlined its proposed purchase by a consortium it was leading. Tri State Corn Processors Cooperative joined Tri-State Financial's objection.

While the trustee's follow-up sale motion was pending, on October 4, 2004, Tri-State Financial filed a motion asking the Court, on shortened notice, to change some of the sale terms established by the September 22, 2004, order. Tri State Corn Processors Cooperative joined Tri-State Financial's motion. Responses were received from Trustee Lovald, EXL, who joined Trustee Lovald's objection in addition to setting forth its own objections, and First Dakota, who opined Tri-State Financial should be compensated, "even if on a quantum merit basis," through the sale process or a subsequent claim allowance.

The Court entered a written decision and denied the motion by order entered October 8, 2004. The Court concluded Tri-State Financial's motion did not raise any arguments it could not have raised earlier when the bidding procedures motion was considered. The Court also responded to each of Tri-State Financial's four requests:

> As noted above, Tri-State Financial's concerns regarding the bidding procedures order were essentially four-fold. Even if these

objections are considered at this late date, they are essentially without merit.

First, Tri-State Financial wants to eliminate all prequalification standards for bidders except for the making of a security deposit. Alternatively, it wants to be allowed to submit financial information about itself other than "CPA audited or reviewed financial statement." As Trustee Lovald aptly stated, the standards for being a qualified bidder for this particular sale of an ethanol plan[t] were designed to insure that the successful high bidder can close the sale within a reasonable time. With such a large sale needing to take place in a relatively short period of time, this requirement is prudent and necessary. Moreover, Trustee Lovald stated that the financial information offered by Tri-State Financial likely will meet the minimum requirements set forth in the bidding procedures order. Thus, Tri-State Financial is not prejudiced solely because it does not have audited financial statements to give the Trustee to become a qualified bidder.

Second, Tri-State Financial wants to delay the closing date to December 1, 2004, and it is willing to assume the expenses of maintaining the plant until closing if it is the high bidder. Had this objection been raised timely, it likely could have been reflected in the bidding procedures order. At this juncture, however, it is too late to make this change, especially where it would be necessary for

Trustee Lovald and other interested parties to identify and quantify the maintenance expenses that would be assumed by the bidder.

Third, Tri-State Financial wants to be deemed a qualified bidder if its offer includes, as a substantial part of the compensation package, waivers of administrative or general unsecured claims against the Chapter 7 estate. Tri-State Financial and Tri State Corn Processors informally raised this objection through their oral arguments at the hearing on the bidding procedures motion. As the Court found on the record at that hearing, a claim waiver bid would not comport with §363(k). Moreover, as the Court previously stated, these administrative or general unsecured claims that would be waived must first be valued through appropriate litigation. Consequently, Tri-State Financial in its Motion to Amend has not identified what manifest error of law or fact the Court made in concluding that cash-only bids, except as modified by § 363(k), would be accepted.

Fourth, Tri-State Financial wants the bid procedures order modified to allow Trustee Lovald significant discretion in deciding whether Tri-State Financial has the ability to close a sale by December 1, 2004, and if so satisfied, to not require it to provide other financial information. As Trustee Lovald has explained, that is precisely what the bidding procedures order now does. The order states that Trustee Lovald will advise potential

> bidders of the minimum financial information required, and he will request more if he needs it. Under the minimum financial standards, audited financial statements are not required if the accuracy of the statement is attested to by the bidder or its representative. Thus, the order already provides for what Tri-State Financial has requested.

In re Tri-State Ethanol Company LLC, Bankr. No. 03-10194, slip op. at 9-11 (Bankr. D.S.D. Oct. 8, 2004).

By order entered *sua sponte* on October 18, 2004, the October 22, 2004, in-court auction was rescheduled to October 26, 2004. The undersigned had a family emergency.[5]

On October 18, 2004, ICM filed an application for allowance of an administrative expense for the re-engineering of the plant, work which it said Debtor had requested in the ordinary course of its business. On October 26, 2004, the Court granted ICM's request for limited notice but also sought an amended application with some changes to the attached itemization. The Court also cautioned counsel the Chapter 11 debtor-in-possession had not obtained authority for ICM to incur the subject post-petition expenses. ICM filed an amended application on November 17, 2004. It stated, "While in Chapter 11, the debtor in possession and other parties in interest, requested [ICM] to

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[5] The undersigned's mother passed away on October 18, 2004.

re-engineer [the] plant." ICM stated it had already received $1,190,000.00 from Tri-State Financial for its post-petition work "to remedy a multitude of engineering problems with the ethanol plant," and it sought another $2,324,466.12 as an administration expense. It stated its "contribution was necessary to preserve the estate and made a substantial contribution to it" by increasing its production capacity of the ethanol plant. In the amended application, ICM further stated it

> regrets having completed this work without having first obtained the approval and protection of a Court order granting it a super priority under the Code. It asks the Court to make an equitable award based on *quantum meruit*, or, the entry of such *nunc pro tunc* orders as may be necessary to insure that ICM, Inc. (characterized by several parties as the "White Knight" in this case) be treated with fundamental fairness.

Amended Application for Allowance of Administrative Expense, pp. 1-2, by ICM, Inc. (Nov. 17, 2004) (file doc. 1137). Trustee Lovald and North Central both requested ICM's administrative expense claim be deferred until after the plant sale closed. At a hearing on the matter held February 8, 2005, which was just after the plant was sold to Tri-State Financial, ICM withdrew its amended application because it felt its claim could now be paid as a general unsecured claim.

At the October 26, 2004, in-court auction, ABUS, L.L.C., was the successful high bidder at $28 million on agreed sale terms, which changed in noted respects during the long hearing. In his affidavit in support of his objection to Tri-State Financial's instant recusal motion, Trustee Lovald adeptly described what happened on the sale day and what transpired thereafter, all of which resulted in Tri-State Financial's being the successful purchaser of the ethanol plant on February 4, 2005, for $27,900,000:

> 3. Trustee filed a motion with the Court to approve a set of bid procedures to be followed by all parties wishing to bid on the plant.
>
> 4. One of those procedures was that once the high bidder was identified, the sale must close within 30 days of the approval of the sale.
>
> 5. Trustee was expending cash funds of approximately $60,000 per month to maintain the plant, and to maintain security at the plant, preparatory to the closing of the sale.
>
> 6. Trustee requested the 30 day closing requirement because that was the approximate time that Trustee estimated that the estate would run out of funds to pay for plant preservation and security. Other than the fact that the estate would run out of funds, there was no major significance associated with picking that date for the closing of the sale.
>
> 7. The morning wrangling that Affiant Larsen refers to was an exchange between Attorney

James Canon [sic], who represented one of the three potential bidders, EXL Group, who was requesting a clarification from the Court that the form contract that had been submitted by EXL with the lead bid for the sale of the plant contained a 'performance guarantee'.

8. The procedure that had been followed by Trustee with respect to the initiation of the bid process was to obtain a lead bid, which in this case was submitted by the EXL Group for $18,800,000 plus an offer on the part of the EXL Group to pay $1,500,000 to ICM for the post-conversion work in completing the plant retrofit. In other words, the opening bid submitted for the plant by the EXL Group was $20,300,000. The matrix of a proposed contract was included within the bid.

9. Attorney Carlon was pointing to certain phrases within the attached contract matrix in claiming that those words created a performance guarantee on the part of the contractor ICM as well as the Chapter 7 Estate. Trustee's position was that no such performance guarantee had been offered as part of the bid process and after extensive exchanges and arguments over the course of the mornings session it was so determined. Attorney Carlon then announced that the EXL Group would not be an active bidder. The performance guarantee issue had never been raised before by Attorney Carlon in any discussions with the Trustee. In several telephone conferences with Attorney Carlon the day prior to the bid hearing process, Attorney Carlon had stated that his client was ready, willing and able

to "blow the competition away" during the course of the bidding process, it came as a complete surprise to Trustee that the EXL Group was not willing, able or prepared to participate in an open bidding process for the sale of the plant.

10. After the morning session, that left the Chapter 7 Estate with two potential bidders Tri-State Financial and ABUS. ABUS indicated to the Court that the requirement that the successful party would have to close the sale within 30 days of approval presented an impediment with its potential lenders in that it would not be able to bid if the closing date remained firm for that time frame. ABUS indicated it would need 15 more days, to approximately December 15, 2004 to be prepared to close the sale. That announcement presented a serious problem for the Chapter 7 Estate inasmuch as it indicated that there would be only one bidder at this sale who was ready, willing and able to bid, which would be Tri-State Financial, and that Tri-State Financial would only be required to bid the first increment above the $20,300,000 bid which would bring the estate $20,400,000 for the sale of the plant. Trustee was aware that a sale at that level would not allow any payment, based on the projections at the time for unsecured creditors of the estate which were identified in the neighborhood of $5,000,000 to $6,000,000. During the course of the afternoon session, during a recess, Trustee and his attorney encouraged ABUS to make a "non-qualified bid" at a level considerably above the lead bid submitted by the EXL Group. That bid was presented at the level of $25,000,000 with a contingency that the closing date be

moved to December 15, 2004. Trustee and Trustee's attorney announced to the Court that because of the substantial increase in funds to the estate offered by that bid, that Trustee was prepared to withdraw the Sale Motion and re-notice the higher bid because it was clearly in the interest of all creditors of this bankruptcy estate to obtain the maximum dollar return for the sale of the plant.

11. The Court did not "force" Tri-State Financial or its representatives to agree to different terms for the bidding process. When Trustee announced that he was prepared to withdraw the Sale Motion, because of the substantially higher offer received for the plant, David Nadolski, as the attorney for Tri-State Financial, announced in open Court, on the record, that Tri-State Financial was ready, willing and able to finish the bidding process and was agreeable to a 15 day extension of the closing date to December 15, 2004.

12. It was also agreed by the parties as a part of the bidding process that the successful bidder would advance funds to the Chapter 7 Estate to provide for plant preservation and security from and after November 30, 2004, when the estate's funds ran out.

13. At the bid hearing most people in the courtroom were either affiliated with Tri-State Financial, which was also an investor in the original plant, or were local farmers from the Rosholt area who at the time were supportive of the Tri State Financial effort to acquire the plant.

A good example of that bias is represented by the multiple pleadings which clearly were a fill-in-the-blank form process that were filed prior to the bid hearing urging the Court to disallow the sale terms and allow Tri-State Financial to credit bid with filed proofs of claim for the plant. There were also rumors circulating prior to the hearing that ABUS (an Australian group) was going to immediately fire all the local employees, should it acquire the plant.

. . . .

15. There are multiple individuals and businesses in the Rosholt area and beyond that were creditors in this bankruptcy that, had Tri-State Financial been the successful bidder for the plant at the level of $20,400,000, would have received nothing on their unsecured claims. Trustee, and the Court *in* its supervisory role, both had a duty to maximize the return to all creditors in this bankruptcy. The actions taken at the hearing, which were all consented to by Tri State Financial, were taken to achieve that result. Had Tri-State Financial not agreed to the extended closing date Trustee would have withdrawn the Sale Motion. Trustee had no duty to Tri-State Financial to act in a manner detrimental to the unsecured creditors in proceeding with a bid process where three bidders had indicated a willingness to bid, but only one was prepared to proceed.

. . . .

17. Trustee does not recollect that the time for the retention of the bid deposits that were required by the three bidders on the plant was a

major bone of contention Trustee does recall that the bid deposit submitted by Tri-State Financial was timely returned to Tri-State Financial, prior to the scheduled ABUS closing in December 2004.

18. ABUS was required to close this sale by December 15, 2004. The day before the scheduled closing Trustee was contacted and advised by the attorney for ABUS that a glitch had occurred in regard to the lenders providing the financing and that ABUS would be delayed in closing the sale by approximately 10 days. Trustee advised ABUS that Trustee could do nothing to extend the closing date, at which time ABUS filed a motion with the Bankruptcy Court to extend the date to close by a short period of time

19. Tri-State Financial objected to the extension, and at the short hearing held by the Bankruptcy Court with regard to the motion for extension, the Court informed ABUS that an extension would not be allowed inasmuch as Tri-State Financial announced at that hearing that it was ready, willing and able to close the sale on the same terms provided that the Court give it an equivalent amount of time to prepare for closing. Without any hesitation the Court agreed to do so, and allowed Tri-State Financial an opportunity to close the sale on or before February 4, 2005.

. . . .

21. When Tri-State Financial encountered problems with the lender it had identified as the source of funds to acquire the plant, the Court clarified for Tri-State Financial and the parties that although February 4th fell on a Saturday,

and was not on a business day, that Tri-State Financial could close the plant sale through the delivery of appropriate funds to Trustee on the appointed date of February 4, 2005.

22. When Tri-State Financial's financing fell through on the afternoon of Friday, February 3rd, Trustee and Trustee's attorney worked with Tri-State Financial to insure that if Tri-State Financial could procure back-up closing finds by the next day, that the sale would be closed in Sioux Falls, South Dakota as opposed to Minneapolis, which was the location of Tri-State Financial's original lender. That process was successfully completed on the afternoon of Saturday, February 4, 2005.

Affidavit of John S. Lovald, ¶¶ 3-22 (pertinent paragraphs) (July 20, 2006) (attachment to file doc. 1893).

In late 2004 and early 2005, while the sale of the ethanol plant was being finalized and some attendant motions regarding the sale were resolved, Trustee Lovald obtained court authority to transfer certain executory contracts to the eventual purchaser. He also sought and obtained authority to disburse a portion of the expected sale proceeds to certain secured creditors holding undisputed claims and the IRS on an administrative claim and to remove judgments from the estate's real property that was being sold. As part of the agreement among the active parties regarding the disbursement of sale proceeds, it was also determined Trustee Lovald should set aside $5,800,000 for payment of North Central's claim once the final claim amount was determined.

After the sale, final orders were able to be entered only on some professionals' fee applications and Trustee Lovald's motion to pay two more secured creditors. Otherwise, administration of the case soon bogged down. North Central commenced litigation against Tri-State Financial in federal district court over the settlement that had been reported to the Bankruptcy Court on June 21, 2004. Both North Central and Tri-State Financial filed vehemently-objected-to applications, motions, and claims regarding what they each thought they were owed from the bankruptcy estate. They each filed different discovery and procedure-related motions that resulted in additional forays. Trustee Lovald commenced an adversary proceeding against Tri-State Financial, Adversary No. 05-1006, seeking a determination Tri-State Financial's post-petition claim should be considered a capital contribution and any allowed claim should be subordinated.

The Court scheduled a joint trial in Adversary No. 05-1006 and the pending contested matters regarding Tri-State Financial's claim for May 2 and 3, 2005. The scheduling order was entered March 23, 2005. Tri-State Financial challenged the Court's authority to combine the matters for hearing, and it sought a delay in the May hearing because: a key witness, James Jandrain, was unavailable to prepare until after the tax season ended April 15, 2005; Jandrain and Tri-State Financial's attorney, Jerrold Strasheim, were preparing for an April 26, 2005, mediation before federal Magistrate Judge John E.

Simko on the federal district court matter between North Central and Tri-State Financial; Attorney Strasheim needed to attend some depositions on other issues in the bankruptcy case; Attorney Strasheim was scheduled for a vacation between May 12, 2005, and May 24, 2005; and Attorney Strasheim had a trial in Nebraska on June 2 and 3, 2005.

By letter decision entered March 31, 2005, the Court denied Tri-State Financial's motion to reschedule, primarily because the Court had advised counsel on March 2, 2005, of its intention to combine any subordination adversary proceeding with the pending contested matters regarding Tri-State Financial's claim and because the issues to be litigated had been on the table for some time. The Court also denied the request because it did not have alternative open court dates available within the next few months.

In part because of a delay in completing discovery due to Attorney Strasheim's law partner's spouse's death and in part because later dates became open, the Court subsequently rescheduled the May 2 and 3, 2005, joint hearing on Adversary No. 05-1006, and the contested matters regarding Tri-State Financial's claim to May 11 and 12, 2005.

Less than a month before the rescheduled hearing date, North Central moved to intervene in both the adversary and contested matters. The Court set a deadline for responses, which were received from Trustee Lovald, Tri-State Financial, and Tri State Corn Processors Cooperative. A written decision was

entered May 4, 2005. The Court denied the motion because an intervention would delay the matter, North Central's interests were adequately represented by Trustee Lovald, and the litigation would not alter any party's equity position in Debtor, which was one of North Central's significant concerns. No appeal was taken, but a month later North Central asked the Court to reconsider.

At the May 11, 2005, hearing on the contested matters related to Tri-State Financial's claim and related Adversary No. 05-1006, appearances were made by Robert E. Hayes for Trustee Lovald and Attorney Strasheim for Tri-State Financial. Attorney Hayes reported a settlement had been reached with Tri-State Financial that would be reduced to writing and noticed for objections. Attorney Strasheim confirmed Attorney Hayes' report.

Trustee Lovald's settlement with Tri-State Financial was noticed for objections on May 17, 2005. It provided Tri-State Financial would be allowed a Chapter 11 administrative expense of $793,654.42 for advances it made to Debtor between May 23, 2003, and July 28, 2004, and it would have a general unsecured claim of $1,190,000.00 for its post-conversion advances. The $1,190,000.00 would be paid after all other timely filed general unsecured claims were paid. The only objector was North Central Construction.

While the settlement motion regarding Tri-State Financial's claim was pending, three contested

matters dealing with the allowance of North Central's claim were also placed on the table.[6] After some delays for discovery and a possible settlement, the contested matters regarding North Central's claim were set for an evidentiary hearing on August 29, 2005.

On June 10, 2005, Tri-State Financial commenced an adversary proceeding, No. 05-1009, against Trustee Lovald and North Central. It sought a determination that North Central's liens should be transferred to the bankruptcy estate and North Central's claim should be treated as unsecured and equitably subordinated to all other general unsecured claims.

On June 15, 2005, the Court directed Trustee Lovald to file an interim report detailing the estate's funds on hand and the list of claims yet unpaid. The Court also directed Debtor to provide a current list of equity security holders as an amendment to document 82, the initial report of equity holders.

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[6] These matters, all pending, are: North Central's April 13, 2005, *Motion to Authorize Payment of Claim*; Trustee Lovald's April 19, 2005, objection to North Central's proof of claim; and Tri-State Financial's April 28, 2005, objection to North Central's proof of claim. [Note: Tri-State Financial's objection to North Central's proof of claim, which was combined with an objection to a motion, is out of sequence on the docket. The Clerk's office had to do some corrective docketing so the objection to claim was appropriately recognized as a separate contested matter on the electronic docket.]

On June 24, 2005, Trustee Lovald reported he was holding $11,527,312.42 in proceeds from the sale of the ethanol plant. He listed the claims he had already paid, which totaled $16,888,317.63, and he estimated he needed $14,709,765.11 to pay all claims in full, including Tri-State Financial's subordinated claim and the untimely filed claims.

On June 24, 2005, Debtor reported the equity holders were: Tri-State Financial, 40.3%; Tri State Corn Processors Cooperative, 27.5%; North Central, 16.1%; and Williams Bio-Energy, 16.1%. Debtor further stated a group of investors transferred their individual interests to Tri-State Financial on June 17, 2003, and no other assignments or transfers had occurred thereafter.

On July 7, 2005, Trustee Lovald asked the Bankruptcy Court to allow him to bring Gaylor Engineering into Adversary No. 05-1009 by third-party complaint or for the Court to abstain from hearing that adversary and allowing the parties to return to state court. The Court denied the trustee's motion the same day because of the timing and because the adversary did not lend itself to a third-party complaint against Gaylor Engineering. The denial was without prejudice to an objection by Trustee Lovald to Gaylor Engineering's proof of claim and without prejudice to Trustee Lovald's commencing an adversary proceeding against Gaylor Engineering so the validity, priority, and extent of any lien claimed by Gaylor Engineering could be resolved. Trustee Lovald commenced an adversary proceeding against Gaylor

Engineering on July 13, 2005, Adversary No. 05-1011. He voluntarily dismissed it a month later.

In early July 2005, Tri-State Financial filed a motion seeking an order compelling North Central to produce certain records related to earlier insurance litigation surrounding the plant construction and subsequent explosion. That motion is still pending due to subsequent settlement proposals, discussed below.

Trustee Lovald reached a settlement with Aux Sable on its executory contract claim and noticed it for objections on July 11, 2005. No objections were filed, and the motion was granted.

Trustee Lovald also reached a settlement with Murphy Trust on its claim and noticed it for objections on August 25, 2005. Tri-State Financial objected on the grounds a condition of liability had not been met by Murphy Trust regarding one of the subject notes. After an evidentiary hearing was set, the parties agreed to submit the matter on stipulated facts and briefs. The matter is still under advisement. A decision has been delayed twice by reported global settlements that the Court understood (apparently incorrectly the first time) would also resolve Tri-State Financial's objection to Trustee Lovald's proposed settlement with Murphy Trust. A decision has subsequently been delayed by the instant recusal motion.

Magistrate Judge John Simko reported to the undersigned he had conducted a mediation on July

26, 2005, that had resulted in a settlement of the three contested matters regarding North Central's claim set for hearing on August 29, 2005. On the parties' behalf, he requested time for them to document their agreement and asked that the August 29, 2005, hearing be cancelled. Based on that report, the Bankruptcy Court cancelled the August 29, 2005, hearing and waited for the settlement to be filed and noticed for objections. A settlement was not timely filed.

A telephonic hearing on an earlier-filed objection by Trustee Lovald to Gaylor Engineering's proofs of claim was held November 8, 2005. Appearances included Trustee Lovald, his counsel, counsel for Tri-State Financial (telephonic), counsel for North Central (telephonic), and counsel for Gaylor Engineering. Counsel for Trustee Lovald and Gaylor Engineering advised the Court the mediated settlement, which the parties were having difficulty reducing to writing, included a provision that assigned to Tri-State Financial the estate's claim against Gaylor Engineering. Counsel for Gaylor Engineering expressed some concerns about that proposal, including the trustee's ability to assign the claim, the lack of identifiable consideration to the bankruptcy estate for the assignment, indemnity issues, and the possible loss of counterclaims or defenses. Counsel for Trustee Lovald reported unresolved indemnity provisions in two sections were the main roadblocks to the parties' efforts to memorialize the mediated settlement, and he discussed how that problem tied into his attempts

to settle Gaylor Engineering's claim. Some options for the disposition of Gaylor Engineering's claim and the indemnity issues were discussed. Counsel for North Central stated it was their position the mediated settlement was binding as made July 26, 2005. No parties took issue with the Court's questions and statements about the present status of the mediated settlement. Ultimately, the Court stated it appeared the parties were close to "being on the same page." The hearing was continued to November 18, 2005. The Court advised the parties that if the mediated settlement were not finalized within those ten days, then on November 18, 2005, the parties and Court would discuss how to proceed.

Shortly before the November 18, 2005, continued hearing on Gaylor Engineering's claim, counsel for North Central sent the Court a letter and several attachments. It was not considered or treated as a filed document.

At the continued hearing on Gaylor Engineering's proof of claim held November 18, 2005, the sole topic was the parties' inability to memorialize the mediated settlement and North Central's desire to push the matter for court approval. Attorney Strasheim, counsel for Tri-State Financial, referenced the recent letter North Central had written the Court, which with attachments totaled 44 pages. The Court advised the parties he had "not had time to go through it." According to Patrick Lee-O'Halloran, counsel for North Central, the attachments included a "transcript of the settlement as read into the record" and

"the latest draft of the agreement." Attorney Strasheim stated his objection to North Central's letter and the inappropriateness of that type of communication with the Court. The Court responded stating any effort to enforce the mediated settlement would have to be done by motion and a hearing. Counsel for North Central stated he wrote the letter because he and Trustee Lovald had "some disagreements" as to "what the procedure is and what the law is in terms of your enforcement of the agreement." He reiterated his opinion the parties had mediated a binding and enforceable agreement before Judge Simko. The Court stated any motion to approve would need to be filed by Trustee Lovald under Fed.R.Bankr.P. 9019 but any party could bring a motion to compel the trustee to recognize the settlement. The parties rehashed some of their arguments from November 8, 2005, regarding what issues remained after the mediated settlement. The Court advised counsel, and counsel for Tri-State Financial in particular, sanctions would be considered if meritless obstructions or objections to the finalization of the settlement were demonstrated. Counsel for Tri-State Financial took exception to the Court's comments, but the Court noted Tri-State Financial had now backed away twice from settlements announced on the record. Counsel for Tri-State Financial again took exception. Ultimately, it was decided the parties should again try to mediate their remaining differences before Judge Simko.

On November 21, 2005, North Central filed a *Motion to Enforce Mediated Settlement Agreement.* Therein, it argued the parties had reached an enforceable agreement through Judge Simko's mediation, and Trustee Lovald should be compelled to notice that settlement for objections. In its supporting brief, North Central stated only an indemnity issue remained before the parties would have a written agreement. It argued Tri-State Financial should not be allowed to use that dispute to undo the agreement the parties recited on the record in front of Judge Simko at the conclusion of the mediation.

On December 14, 2005, Tri-State Financial objected to North Central's motion. It argued a final agreement was never reached. It also contested this Court's jurisdiction on "specific performance" grounds and because some of the mediation had addressed the District Court lawsuit between North Central and Tri-State Financial in addition to the contested matters and related adversary proceedings before the Bankruptcy Court. Tri-State Financial also complained North Central had improperly disclosed settlement discussions to the Bankruptcy Court, most notably in the letter the Court received from North Central just before the November 18, 2005, continued hearing on Trustee Lovald's objection to Gaylor Engineering's claim.

Also on December 14, 2005, Trustee Lovald filed a response to North Central's *Motion to Enforce Mediated Settlement Agreement.* He acknowledged a provision regarding an indemnity provision had kept

the parties from completing a written stipulation. Trustee Lovald also opined, contrary to North Central's assertions,

> the agreement reached at the mediation is too imprecise for this Court to enforce. The specific language of the disputed indemnity provisions is not contained in the mediation transcript. Further, the negotiations that have occurred during the drafting process have resulted in an impasse over the indemnification language. Applying basic rules of contract formation, there is simply no agreement to be enforced against any of the parties.

Trustee Lovald also noted in his response "several of the agreements reached at the mediation required further expansion and clarification" and "terms of the written agreement have moved well beyond the scope of the 'core agreements' recited at the conclusion of the July 26, 2005 mediation." It urged the Court not to let North Central use the pending motion to "bootstrap" into an agreement the precise indemnification language that North Central wanted.

The parties attempted another mediation with Judge Simko in early December 2005 to iron out remaining differences. Again, the parties left without a written agreement, and they were not able to achieve one thereafter. By order entered January 20, 2006, an evidentiary hearing on North Central's *Motion to Enforce Mediated Settlement Agreement* was set for February 9, 2006. On February 2, 2006,

in anticipation of the evidentiary hearing and to recognize the concerns Tri-State Financial had about North Central's disclosure of settlement discussions, the Court sealed the July 26, 2005, mediation transcript until further order.

Following a dyspeptic pre-hearing conference with counsel for interested parties on February 6, 2006, an evidentiary hearing on North Central's *Motion to Enforce Mediated Settlement Agreement* was held before the Bankruptcy Court on February 9, 2006. At the outset, Attorney Strasheim, counsel for Tri-State Financial, sought, with one exception, an order barring as evidence "any part of any record of the mediation proceedings on either July 26th or December 8th of last year[.]" He stated he did not know the Court had sealed the transcript earlier. During a colloquy with the Court regarding Federal Rule of Evidence 408 and its impact, Attorney Strasheim suddenly announced Tri-State Financial did "not oppose enforcement of [the] core agreements" reached at the July 26, 2005, mediation and "there were things that were not agreed to and those would be the things that could not be enforced." Attorney Strasheim argued at length his personal written understanding of the July 26, 2005, mediation results constituted eleven "core agreements" Tri-State Financial was agreeable to having the Court enforce. He took great exception to the Court's finding that the core agreements from the mediation would be whatever the parties had recited and affirmed on the record with Judge Simko at the conclusion of the July

26, 2005, mediation. The hearing was recessed so the Court and interested parties could review the sealed transcript. When the hearing continued, the parties offered no meaningful argument that the transcript included the negotiations leading to their settlement or that it represented anything other than their consensus, *i.e.*, there was nothing Judge Simko had ordered them to do. Accordingly, the Court concluded the transcript contained only the results of the parties' mediation and was therefore admissible. The Court also stated the simplest resolution of the matter was to have Trustee Lovald file a motion to approve the mediated agreement and attach the transcript as the record of that agreement.[7]

Attorney Strasheim continued to argue the transcribed agreement was not enforceable for various reasons, and he also publicly expressed his concern whether the undersigned "has been a neutral unbiased fair tribunal as far as [Tri-State Financial] is concerned[.]" In particular, he relayed concerns about the short answer period the Court had set in Adversary No. 05-1006 and the Court's denial of continuances requested by Tri-State Financial in connection with the auction sale of the ethanol plant. Counsel for Tri-State Financial then renewed Tri-State Financial's objection to the Bankruptcy Court's subject matter jurisdiction and continued arguing he,

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[7] During this hearing, the Court erroneously referred to the mediated settlement of July **28**, 2005, instead of July **26**, 2005.

and apparently his client, would not recognize the record made at the conclusion of the July 26, 2005, mediation as the best record of the "core agreements" reached that day. He further argued some of the agreements reached that day were unenforceable due to lack of specificity. Following additional arguments by counsel for Tri-State Financial and other parties, the Court unsealed the transcript of the mediation results, again stated it was accepting the transcript as the record of the agreement the parties made on July 26, 2005, and directed Trustee Lovald to notice the agreement for objections. The Court indicated enforceability of the agreement could be raised later.

Nonetheless, Attorney Strasheim renewed his objection that the transcript contained privileged matters. Attorney Strasheim next wanted admitted "twenty drafts and these e-mails," that apparently were exchanged between the parties after July 26, 2005, but he also wanted to "reserve the right to, to the privilege of them because I think that they complete the picture." After the Court stated Tri-State Financial would need to waive the privilege if it wanted the documents admitted, Attorney Strasheim stated the post-mediation documents should be considered under the Rule of Completeness. He also argued the mediation results transcript contained other statements, admissions, and language and, though he could not specifically identify them in the transcript, he did not agree these other parts were admissible. Attorney Strasheim then again offered his own written rendition of the "core agreements." The

Court restated its previous ruling that the transcript was the best memorialization of the mediation results. Some colloquy followed on the impact of subsequent negotiations on the "core agreements," but there was no dispute the core agreements were never formally rescinded by the parties. A short recess was taken to allow Attorney Strasheim to present any other evidence he had. After the break, he again sought admittance of a large number of exhibits (A through VVV) that apparently included written exchanges between the parties *after* the July 26, 2005, mediation. North Central objected on grounds of relevance, authentication, and hearsay. The Court sustained the objection on relevance. Attorney Strasheim presented the documents again on an "offer of proof," which the Court did not understand.[8] He next moved to dismiss North Central's motion, which was denied, and then asked the Court for an extended time in which to file an appeal, which was also denied. The Court offered to submit proposed findings and conclusions to the District Court to alleviate any concerns regarding the Court's jurisdiction over that portion of the mediation agreement involving the District Court matter between North Central and Tri-State Financial. In response, Attorney Strasheim said "I am not insisting on the Court do that with respect to that one issue," but he still

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[8] The Court took Tri-State Financial's Exhibits A through VVV on this "offer of proof" but did not review them. The exhibits are still in the hands of one of the appellate courts.

said he was objecting to "subject matter and core jurisdiction." The Court clarified its ruling and stated it was only ruling an agreement had been reached on July 26, 2005; the Court left it to Trustee Lovald to decide whether to seek approval of the mediated agreement. During the following week, the parties wrangled over the proposed dispositional order. An order was eventually entered on February 21, 2006. Tri-State Financial appealed the order on February 23, 2006.[9]

On February 21, 2006, Trustee Lovald filed his motion to approve the mediated settlement. It was followed by an amended motion on February 24, 2006, that better set forth the several contested matters and adversary proceedings the settlement purported to resolve. Two objections were filed. Tri-State Financial objected[10] raising several of the same

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[9] The United States District Court for the District of South Dakota, the Hon. Charles B. Kornmann, dismissed the appeal on April 12, 2006, as "being totally without merit" and for lack of jurisdiction over the Bankruptcy Court's interlocutory order regarding the mediated settlement. The District Court remanded for further proceedings, "including any consideration of awarding terms or costs in connection with the filing of the appeal." To date, no parties to the appeal have sought terms or costs. Tri-State Financial appealed Judge Kornmann's ruling to the United States Court of Appeals for the Eighth Circuit on April 27, 2006. That appeal was dismissed on Tri-State Financial's motion on May 22, 2006.

[10] Trustee Lovald took issue with Tri-State Financial's standing to object based on terms of the mediated settlement. The challenge was dismissed as untimely, but the Court noted the mediated settlement nonetheless included terms that

(Continued on following page)

objections it had made at the February 9, 2006, hearing. Though the mediated agreement had not yet been court-approved, Tri-State Financial also argued North Central and Trustee Lovald had breached the agreement. Gaylor Engineering objected because the settlement purported to sell to Tri-State Financial a "perceived cause of action [held by the bankruptcy estate] against Gaylor" but Trustee Lovald had not shown the consideration for that sale nor shown how a sale to Tri-State Financial rather than a public auction was in the estate's best interest. Gaylor Engineering said the mediated settlement was also prejudicial to it because the settlement did not clearly preserve its ability to assert against Tri-State Financial "all available defenses and the concomitant counterclaim for payment."

An evidentiary hearing was held May 4, 2006. Trustee Lovald was the only witness. The only exhibits were the July 26, 2005, mediation results transcript and a May 1, 2006, statement by Trustee Lovald of the remaining claims against the estate. Trustee Lovald estimated that day that he had sufficient funds to pay 95% of the unsecured creditors' claims.

The Court denied approval of the settlement, in part because of the proposed assignment of the

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precluded Tri-State from later objecting to it, which the Court could recognize independent from Trustee Lovald's late-filed objection to Tri-State Financial's standing.

estate's claim against Gaylor Engineering to Tri-State Financial, for which Trustee Lovald was unable to identify or quantify the consideration to be given by Tri-State Financial. The Court also concluded the proposed settlement was unreasonable because it inexplicably moved Tri-State Financial's previously subordinated unsecured claim, as was provided in the trustee's May 2005 proposed settlement with Tri-State Financial, into the class of general unsecured claims. The Court was unwilling to recognize this improved status for Tri-State Financial's $1,190,000 unsecured claim for two reasons. First, the claim had arisen from post-petition re-engineering work at the ethanol plant the Court earlier had not authorized. Second, Trustee Lovald had estimated the class of unsecured claim holders would face a shortfall. Some colloquy followed regarding the estimated amount of any shortfall. The Court concluded Trustee Lovald had failed to demonstrate the proposed assignment to Tri-State Financial of the estate's claim against Gaylor Engineering was reasonable. Though his retirement was pending, the Court also advised the parties of his intentions to finish the case.

The next long-pending matter taken up for hearing by the Court, following its disapproval of the mediated settlement, was Trustee Lovald's May 17, 2005, proposed settlement with Tri-State Financial.[11]

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[11] The hearing was rescheduled once to accommodate a vacation trip taken by Attorney Strasheim.

North Central, the lone objector, withdrew its objection as the June 13, 2006, hearing commenced. The Court nonetheless asked Trustee Lovald to make his record in support of the settlement.

Before the trustee's presentation started, Attorney Strasheim announced Tri-State Financial was preparing a motion asking the Court to recuse itself. Attorney Strasheim explained he was making the announcement to avoid "sandbagging" complaints and because he did not want to wait to make the announcement until it was known whether it would get a favorable ruling on the proposed settlement. He stated Tri-State Financial intended to ask the Court to recuse itself "from anything that we're a party [to] or that effects [sic by transcriptionist] us."

Testimony and two exhibits from Trustee Lovald were received. The Court approved Trustee Lovald's May 17, 2005, settlement with Tri-State Financial.

First Dakota added to the post-sale litigation by initiating two contested matters. The first was filed in early April 2005 when First Dakota requested attorneys' fees and other costs under § 506(b). Following a hearing, the Court received closing arguments in mid-July 2005 and entered a written decision September 27, 2005, allowing First Dakota $180,706.20 of the $195,076.15 it sought.[12] The second was filed in

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[12] A subsequent request by First Dakota for the Court to amend the decision is still pending, in part because the related motion by First Dakota for payment of a pre-payment penalty is also pending.

early August 2005 when First Dakota sought an additional $173,253.27 under § 506(b) as a pre-payment charge. Objections were filed by Tri-State Financial. It argued the charge was not enforceable under South Dakota law or federal bankruptcy law. It also argued First Dakota had breached "its duty of good faith and fair dealing" with Debtor under the original loan and by such material breach, Debtor was discharged from any liability on the pre-payment penalty. Trustee Lovald filed an objection and appeared to have been a bit blindsided by First Dakota's request, in light of the full payment with interest on First Dakota's note and the pending attorneys' fees motion under § 506(b). He, too, argued federal bankruptcy law rendered the penalty unenforceable. Greenway Consulting, L.L.C., also filed an objection but withdrew it when the matter came up for hearing.

Trustee Lovald eventually reached a settlement with First Dakota on the pre-payment penalty. Tri-State Financial objected, and a hearing was held March 24, 2006. Based on the Court's preliminary findings, Trustee Lovald withdrew his settlement motion. That put First Dakota's original request for the payment back on the table. An evidentiary hearing was held May 4, 2006. The matter was taken under advisement.

More routine matters in the case were also addressed in late 2005 and the first half of 2006. In early September 2005 and again in late January 2006, Trustee Lovald filed several objections to the

claims of more minor parties. Most were easily resolved; either the creditor did not respond to the objection, or Trustee Lovald withdrew his objection after further discovery.

Trustee Lovald's objection to the proof of claim filed by Western Biomass Energy, L.L.C. ("Western Biomass"), required an evidentiary hearing. Western Biomass had sought $33,350.33. Trustee Lovald objected, saying corporate records did not support the amount of the claim and a contract clause regarding payment of a bonus had never been authorized by Debtor. An evidentiary hearing was held October 12, 2005. The Court received four exhibits and the testimony of Randy Kramer, one of two shareholders of Western Biomass. At the hearing, Trustee Lovald stated he was challenging only $17,500.00, which represented the bonus portion of the total claim. On examination, Kramer acknowledged Debtor's board of directors had never officially assumed Tri State Corn Processors Cooperative's liability to Western Biomass. The Court, therefore, sustained the trustee's objection and advised Kramer he might need to look to Tri State Corn Processors Cooperative for payment of Western Biomass' bonus claim. No appeal was taken.

Trustee Lovald's objection to the proof of claim filed by James Jandrain also required an evidentiary hearing. Jandrain, who, as discussed above, holds direct or indirect equity interests in both Debtor and Tri-State Financial, filed a proof of claim for

$53,327.50 for accounting and related services he said he rendered for Debtor pre-petition.[13] Briefs, numerous exhibits, and Jandrain's testimony were received. The trustee's objection was sustained, and the Court adopted his brief as the Court's general findings and conclusions. The Court specifically concluded corporate records indicating Debtor had authorized Jandrain to perform the services for an agreed compensation were insufficient. Jandrain timely appealed the Court's decision on May 11, 2006. The United States District Court for the District of South Dakota, Hon. Charles B. Kornmann, upheld the Bankruptcy Court's decision by order entered August 22, 2006.

On June 20, 2006, Trustee Lovald filed a motion to approve his settlement with North Central. Before the objection period on that motion expired, Tri-State Financial filed a motion asking the Court to allow it to intervene in the contested matter of Trustee Lovald's objection to North Central's proof of claim, despite the fact Tri-State Financial had its own objection to North Central's proof of claim and despite the fact Trustee Lovald had just noticed a settlement of North Central's claim for objections. On June 28, 2006, the Court entered an order holding Tri-State Financial's intervention motion in abeyance pending a resolution of Trustee Lovald's proposed settlement with North Central.

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[13] Jandrain did not file a proof of claim while the case was under Chapter 11.

On June 29, 2006,[14] Tri-State Financial filed a *Motion for Recusal* regarding the undersigned. The Court set July 20, 2006, as the deadline for filing any joinders in or responses to the recusal motion. James Jandrain, Randy Kramer, and ICM joined the motion.

Tri-State Financial set forth six "Basis for Bias," some of which intertwined. It offered one affidavit, that of a Rosholt area newspaper reporter, in support of its motion. The three joinders were all "bare" joinders; none set forth any additional grounds for recusal, and none specifically stated why they had joined Tri-State Financial's motion.[15]

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[14] Mid-morning on June 27, 2006, local counsel for Tri-State Financial, placed a highly imprudent telephone call to the undersigned's chambers in Pierre. He told the undersigned's judicial assistant the undersigned's law clerk could not assist him and he needed to talk to the undersigned on a "personal matter." When the undersigned returned the telephone call, he learned the attorney wanted to speak to him about Tri-State Financial's planned recusal motion. The content of his short, yet ill-advised, conversation with the Court is not included herein nor is it a factor in this Court's decision on the recusal motion.

[15] Local counsel for Tri-State Financial who signed the recusal motion and counsel for the parties who filed joinders to Tri-State Financial's recusal motion have had limited involvement in the case. The Court trusts each of these attorneys obtained and read all relevant pleadings and transcripts and reached an independent conclusion that recusal was warranted. *See* Fed.R.Bankr.P. 9011(b).

Objections were filed by First Dakota and Trustee Lovald.[16] First Dakota opined the Court was able to make objective decisions. It also stated Tri-State Financial "has been extraordinarily litigious, difficult to deal with and otherwise counterproductive throughout the Chapter 7 process." It also stated

> but for the excesses of [Tri-State Financial], all creditors, including [Tri-State Financial], would likely have already been paid. To the extent this Court or the appeals courts have, based on the record of [Tri-State Financial]'s tactics and behavior in this Chapter 7 case drawn, [sic] conclusions unfavorable to [Tri-State Financial], such conclusions are not grounds for recusal.

Objection to Motion for Recusal, pp. 1-2, by First Dakota (July 20, 2005) (file doc. 1892).

In his objection, Trustee Lovald set forth the applicable law and argued Tri-State Financial had failed to show bias and its motion was untimely. He also submitted an affidavit. Therein, he detailed the ethanol plant sale process, including both in and out-of-court discourse among the parties. He further stated he had attended all hearings since the case was converted to Chapter 7 and had "not witnessed any bias against or for Tri-State Financial or its representatives." Trustee Lovald included in his

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[16] Eugene Paulson also submitted a response by facsimile transfer. Since an original, signed document was not received timely, his response could not be considered.

affidavit the reasons he believes the Court had correctly ruled on the objections to the proofs of claims filed by Randy Kramer[17] and James Jandrain. He also stated any argument by Tri-State Financial regarding a return on equity is "reckless and misleading" since any meaningful return to equity holders could only be generated if remaining claims are slashed substantially. Trustee Lovald said any contrary suggestion by Tri-State was a "red herring." He further opined the undersigned "has been fair to all parties involved in this bankruptcy, but does have the overriding motivation to see the estate closed and unsecured creditors paid in a timely fashion." Trustee Lovald also stated:

> This case has reached the point where the only major obstacle preventing final administration of the case is the claim of North Central Construction. Tri-State Financial has been and continues to be engaged in a bitter vendetta with this creditor and appears to want to use the estate, and the estate's resources, to continue the dispute unabated. That course of action could tie up the estate for years to come, and substantially reduce the estate's cash, because of the priority position held by North Central Construction. . . .
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[17] The Court assumes Trustee Lovald was referring to the proof of claim filed by Western Biomass Energy, L.L.C., which was signed by Randy Kramer as its president.

> Trustee respectfully submits that the Motion for Recusal submitted by Tri-State Financial is nothing more than a thinly veiled and stale attempt to judge shop in an attempt to dominate and control all decisions in the administration of this case, and to hi-jack the estate's limited resources to engage in endless litigation with North Central Construction. . . .

Affidavit of John S. Lovald, ¶¶ 36-38 (pertinent parts) (July 20, 2006) (attachment to file doc. 1893). Both Trustee Lovald and First Dakota opined a change of judge at this stage would further delay case administration.

At the time Tri-State Financial filed its recusal motion, several contested matters were pending: the objections to North Central's claim, a motion from North Central seeking payment, and the trustee's proposed settlement of North Central's claim; one discovery related motion and one "intervention" motion by Tri-State Financial regarding objections to North Central's claim; First Dakota's request for payment of a pre-payment penalty (under advisement); First Dakota's motion requesting a clarification and amendment of its § 506(b) claim for attorneys' fees (under advisement); and a fee application by an estate accountant (uncontested); Trustee Lovald's proposed settlement of the Murphy Trust's claim (under advisement); a fee application by one of the Chapter 7 estate's attorneys; and Trustee Lovald's objection to Clapper Corporation's proof of claim.

Of the six associated adversary proceedings, two have been resolved by dismissal, Nos. 03-1053 and 05-1011. Pending are: Adversary No. 03-1032, commenced by North Central on July 14, 2003, which is essentially a continuation of the state court action regarding lien priorities and claim amounts, and which was prematurely reported settled twice; Adversary No. 05-1009, commenced by Tri-State Financial against Trustee Lovald and North Central on June 10, 2005, in which Tri-State Financial seeks a subordination of North Central's allowed claim; and Adversary No. 06-1018, commenced on August 15, 2006, in which Trustee Lovald alleges negligence and breach of contract and seeks indemnity and damages from Gaylor Engineering arising from the initial plant construction.

Also pending are Adversary No. 05-1006, in which Trustee Lovald sought a subordination of Tri-State Financial's claim, and Tri-State Financial's January 24, 2005, administrative expense application. It appears, however, the parties actually resolved or intended to resolve both through the settlement that was approved June 14, 2006. Upon disposition of the instant recusal motion, the Court will clarify these matters with the Clerk and affected parties.

A few days after it filed the recusal motion, Tri-State Financial filed a motion seeking authority to depose Trustee Lovald regarding the recusal motion. Since the recusal motion was pending against the undersigned and since Tri-State Financial had

requested therein that the undersigned not preside over "all litigation of every kind and nature" involving it in this case, the Court referred the deposition motion to the Hon. Robert J. Kressel, Bankruptcy Judge for the District of Minnesota, who is authorized to hear conflict cases. Judge Kressel denied Tri-State Financial's deposition motion. Tri-State Financial then filed a *Motion to Reconsider, Set Aside, Alter and/or Amend Orders*. It challenged the order transferring the deposition motion to Judge Kressel and it challenged Judge Kressel's order denying the deposition motion. Since Tri-State Financial's motion to amend principally challenges Judge Kressel's order, its disposition is also before Judge Kressel.

Even after more than 70 pages, not everything that has transpired in this case and the related adversary proceedings has been reiterated herein. The Court has attempted, however, to provide a sufficiently thorough review of what has transpired to date so it may appropriately consider the recusal motion filed by Tri-State Financial.

II.

Section 455 of Title 28 of the federal code demands that a federal judge recuse himself *sua sponte*. It provides:

> (a) Any justice, judge, or magistrate judge of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.

> (b) He shall also disqualify himself in the following circumstances:
>
> > (1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding;
>
> . . . .
>
> (d) For the purposes of this section the following words or phrases shall have the meaning indicated:
>
> > (1) "proceeding" includes pretrial, trial, appellate review, or other stages of litigation. . . .

28 U.S.C. § 455 (in pertinent part). Section 455 applies to Bankruptcy Court judges. *Smith v. Edwards & Hale, Ltd. (In re Smith)*, 317 F.3d 918, 932 (8th Cir. 2002). The statute was designed to promote public confidence in the impartiality of the judicial process. *Ouachita National Bank v. Tosco Corp.*, 686 F.2d 1291, 1300 (8th Cir. 1982) (cited in *Moix-McNutt v. Coop (In re Moix-McNutt)*, 215 B.R. 405, 409 (B.A.P. 8th Cir. 1997)). Judicial impartiality is presumed, so a party seeking recusal bears a substantial burden to prove otherwise. *United States v. Denton*, 434 F.3d 1104, 1111 (8th Cir. 2006). Whether to recuse himself is committed to the court's sound discretion. *Dossett v. First State Bank*, 399 F.3d 940, 953 (8th Cir. 2005).

Section 455(a) sets forth an objective standard of reasonableness. *United States v. Martinez*, 446 F.3d 878, 883 (8th Cir. 2006). The issue is whether the

judge's impartiality might reasonably be questioned by the average person on the street who knows all the relevant facts of a case. *Id.* (cites therein). In contrast, under § 455(b)(1), actual bias or prejudice must be demonstrated. *O'Regan v. Arbitration Forums, Inc.*, 246 F.3d 975, 988 (7th Cir. 2001).

In essence, a judge need not recuse himself for bias or prejudice if "his knowledge and the opinion it produced were properly and necessarily acquired in the course of the proceedings, and are indeed sometimes (as in a bench trial) necessary to completion of the judge's task." *Liteky v. United States*, 510 U.S. 540, 551 (1994). Opinions garnered from earlier proceedings are also not disqualifying. *Id.* However,

> [a] favorable or unfavorable predisposition can also deserve to be characterized as "bias" or "prejudice" because, even though it springs from the facts adduced or the events occurring at trial, it is so extreme as to display clear inability to render fair judgment."

Id. Some courts have denominated this as the pervasive bias exception to the extrajudicial source doctrine.[18] *Id.* (cite therein). In this Circuit, a pervasive bias is aptly described as "a deep-seated favoritism or antagonism" held by a judge from whatever source

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[18] The doctrine may be better described as a "factor" since the presence of an extrajudicial source does not necessarily establish bias, nor does the absence of an extrajudicial source necessarily preclude bias. *Liteky*, 510 U.S. at 554-55.

"that would make fair judgment impossible." *United States v. Larsen*, 427 F.3d 1091, 1095 (8th Cir. 2005). When a request for recusal is based on a judge's in-court conduct, the requesting party must show "the judge had a disposition 'so extreme as to display clear inability to render fair judgment.'" *Denton*, 434 F.3d at 1111 (quoting *Liteky*, 510 U.S. at 551).

Whether a court is applying § 455(a) or § 455(b)(1), the Supreme Court has provided significant guidance.

> First, judicial rulings alone almost never constitute a valid basis for a bias or partiality motion. *See United States v. Grinnell Corp.*, 384 U.S., at 583, 86 S.Ct., at 1710. In and of themselves (*i.e.*, apart from surrounding comments or accompanying opinion), they cannot possibly show reliance upon an extrajudicial source; and can only in the rarest circumstances evidence the degree of favoritism or antagonism required (as discussed below) when no extrajudicial source is involved. Almost invariably, they are proper grounds for appeal, not for recusal. Second, opinions formed by the judge on the basis of facts introduced or events occurring in the course of the current proceedings, or of prior proceedings, do not constitute a basis for a bias or partiality motion unless they display a deep-seated favoritism or antagonism that would make fair judgment impossible. Thus, judicial remarks during the course of a trial that are critical or disapproving of, or even hostile to, counsel, the parties, or their cases,

> ordinarily do not support a bias or partiality challenge. They *may* do so if they reveal an opinion that derives from an extrajudicial source; and they *will* do so if they reveal such a high degree of favoritism or antagonism as to make fair judgment impossible. . . . *Not* establishing bias or partiality, however, are expressions of impatience, dissatisfaction, annoyance, and even anger, that are within the bounds of what imperfect men and women, even after having been confirmed as federal judges, sometimes display. A judge's ordinary efforts at courtroom administration – even a stern and short-tempered judge's ordinary efforts at courtroom administration – remain immune.

Id. at 555-56 (emphasis in the original); *see United States v. Sypolt*, 346 F.3d 838, 839 (8th Cir. 2003).

Finally, though there is no procedure set forth in § 455, a recusal request must nonetheless be timely. *Fletcher v. Conoco Pipe Line Co.*, 323 F.3d 661, 664 (8th Cir. 2003). For a request to be timely, it must be made "at the earliest possible moment after obtaining knowledge of facts demonstrating the basis for such a claim" *Id.* (quoting *Apple v. Jewish Hospital & Medical Center*, 829 F.2d 326, 333 (2nd Cir. 1987)). If there is a delay, the requesting party has the burden to show good cause for the untimeliness. *Holloway v. United States*, 960 F.23d [sic] 1348, 1355 (8th Cir. 1992).

III.

Tri-State Financial sets forth six "Basis for Bias" in its *Motion for Recusal*. At the beginning of part IV of its recusal motion, Tri-State Financial referenced § 455(a), and at the beginning of part V, it referenced § 455(b)(1) and incorporated by reference all the "allegations" in part IV. Though there is marked duplication of allegations within the six bases, the Court first separately addresses each as to content. The Court then sequentially applies § 455(a), § 455(b)(1), and the Due Process Clause under the collective light of the six bases. Trustee Lovald's objection that the recusal motion was untimely is also addressed.

Basis No. 1

Tri-State Financial argued the Court holds an "insuppressible conviction" Tri-State Financial and the Omaha Group "thumbed their noses at his judicial authority, abused the bankruptcy process, and nefariously schemed to get control of [Debtor]" and the Court's rulings, in particular the Court's denial of Debtor's Motion to Approve Re-engineering Stipulation and the conversion of the case to Chapter 7, have been designed to economically punish them for their behavior. Tri-State Financial also took issue with what it described as "gratuitous" statements by the Court "denouncing" these parties at the July 28, 2004, hearing, where confirmation of Debtor's modified Chapter 11 plan and the United State Trustee's

motion to dismiss or convert were on the table. Tri-State Financial believes a new judge is needed so its claim for the re-engineering of the ethanol plant can be fairly decided.

In this portion of its recusal motion, Tri-State Financial acknowledged Debtor, ICM, and Tri-State Financial proceeded with the re-engineering of the plant at some point before the Court entered its December 12, 2003, decision denying Debtor's September 25, 2003, Motion to Approve Re-engineering. Tri-State Financial said it did so on the advice of in-state counsel and former out-of-state counsel. Tri-State Financial further acknowledged the same parties conferred after the Court's denial and again decided to proceed. It also inferred the Court knew at some unstated date the project had already begun and/or was continuing and the undersigned failed to order Debtor, ICM, or Tri-State Financial to stop the re-engineering project.

It is true the Court denied Debtor's Motion to Approve Re-engineering Stipulation and to incur the attendant debt. As set forth in the December 12, 2003, Decision, the proposal was denied because such "wide-sweeping provisions" are better addressed through a plan confirmation process, Debtor had not met its burden of proof for giving superpriority liens to the creditors involved, some of whom were insiders, and Debtor had failed to show existing creditors were adequately protected. In its discourse in the recusal motion, Tri-State Financial somehow interprets that decision as damning evidence the Court

does not like Tri-State Financial and its principals and attorney, the Court concluded the re-engineering was not a worthwhile project, and Tri-State Financial and its principals should be punished. Such overwrought inferences are not supported by the record and are paranoic in tenor. They also simply ignore Debtor was then in a Chapter 11 bankruptcy in which the goal should have been to financially reorganize the Debtor and pay creditors, not necessarily re-engineer the plant. At neither the hearing on Debtor's Motion to Approve Re-engineering Stipulation nor any subsequent hearing did Debtor or Tri-State Financial make a record that demonstrated the re-engineering was necessary for Debtor to fulfill its Chapter 11 duties and goals.

There is also no legal support for Tri-State Financial's statement the Court should have *sua sponte* stopped the re-engineering project once it learned Debtor was proceeding without appropriate authority.[19] Raising that issue was the prerogative of the United States Trustee or one of the creditors, not the Court.

Several times in its recusal motion, Tri-State Financial stated the re-engineering project was effected without court approval to "preserve" the

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[19] The first indication the Court could find in the record that the re-engineering project had continued was on June 8, 2004. Whether there was any mention of it orally during an earlier hearing is unknown.

"going concern value" of the ethanol plant. That premise, however, cannot be found in Debtor's actual Motion to Approve Re-engineering Stipulation. Instead, in the motion Debtor stated the re-engineering project was necessary for the plant to "operate competitively in the market place" and allow it "to repay creditors and to effectuate a plan absolutely and unconditionally[.]" Why Tri-State Financial is now attempting to recast the purpose of the re-engineering project is unknown.

Finally, Tri-State Financial stated another judge should "resolve any claims that [Tri-State Financial] violated [the undersigned]'s order [date or topic of order not stated]." The statement is pointless. There are no matters pending before the Court in which Debtor's failure to get court authority for the re-engineering project is at issue, and no such issues are expected to arise in the future. Tri-State Financial's claim was resolved by order approving stipulation entered June 14, 2006. Under the approved stipulation, Tri-State Financial will receive $793,654.42 as an administrative expense claim (primarily for payroll, insurance, and other operating expenses and United States Trustee's fees) and $1,190,000.00 as a subordinated general unsecured claim (for payments it made in March 2004 and June 2004 to ICM for equipment). In other words, Tri-State Financial is now assured that it will receive all or nearly all of its

claim arising from the re-engineering project and other post-petition expenses it paid for Debtor.[20]

Basis No. 2

Tri-State Financial claimed a "fully informed person on the street might reasonably also doubt [the undersigned]'s impartiality because he appears to have a deep seated dislike for, distrust of, and antagonism toward [Tri-State Financial] and certain members from the Omaha Group who are important witnesses in the disputes [delineated above]." In support, Tri-State Financial submitted the affidavit of Grace "Mimi" Larsen, a reporter from Rosholt, where the ethanol plant is located, who met with the undersigned following the in-court auction of the ethanol plant on October 26, 2004.

According to Reporter Larsen's affidavit, as summarized in part and quoted in part by Tri-State Financial in its recusal motion, the Court "strongly dislikes and is antagonistic" toward John Hoich, a member of Tri-State Financial and the Omaha Group, "apparently" because Hoich is wealthy and played a role in the re-engineering project "or because [the undersigned] believes that Hoich 'hit on' his clerk." Tri-State Financial's use of the word "apparently" indicates only supposition, which it is, especially as to its erroneous conclusion the undersigned does not like

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[20] Trustee Lovald testified on May 4, 2006, he would have sufficient funds to pay approximately 95% of unsecured claims.

Hoich because he is wealthy or involved with Tri-State Financial, the Omaha group, the re-engineering project, or David VanderGriend. To the extent the Court formed an opinion that Hoich is arrogant because of his demeanor on the witness stand and his questionable conversation with a member of the Clerk's office staff, the Court is justified in having that opinion, regardless of whether the Court actually conveyed those impressions to the reporter. Further, the Court has no recollection of stating to Reporter Larsen that he enjoyed watching Hoich "sweat" during the ethanol plant sale.

Tri-State Financial's concluding statement in paragraph 4.14 of its recusal motion that Tri-State Financial "lost out in its attempt to buy the Ethanol Plant" is a puzzling misstatement of the record. Tri-State Financial was ultimately the successful buyer and closed the sale in February 2005.

Tri-State Financial and Reporter Larsen again relied upon only supposition when they stated the undersigned "appears" to have a "strong dislike for and distrust of James Jandrain" and this dislike "probably" arose from Jandrain's testimony in support of Debtor's Motion to Approve Re-engineering Settlement and his involvement with David VanderGriend. Again, the Court has no personal opinion about James Jandrain, let alone a negative one because he was involved, to an unknown extent, in the re-engineering project or with David VanderGriend.

Tri-State Financial and Reporter Larsen have apparently also concluded, based on Larsen's newspaper interview with the Court, the undersigned has hostile feelings toward Tri-State Financial or its out-of-state counsel, Attorney Strasheim, in whole or in part because Attorney Strasheim is a former bankruptcy judge and may have been employed in this case to foster an advantageous relationship with the Court. The Court has no personal relationship with Attorney Strasheim and has no knowledge of what motivated Tri-State Financial to hire him. Why in-state counsel introduced Attorney Strasheim to the Court as a former bankruptcy judge at Attorney Strasheim's first hearing on June 21, 2004, is also unknown, but to surmise the Court was negatively disposed to Tri-State Financial or Attorney Strasheim thereafter is a *non sequitur*.

Tri-State Financial made erroneous and ill-founded conclusions when it stated the Court "implicitly, if not explicitly, accused important witnesses associated with [Tri-State Financial] and the Omaha group of not being truthful." Tri-State Financial's only accurate statement in paragraph 4.16 of its recusal motion is that the Court stated in its December 12, 2003, decision that Debtor's proposed re-engineering settlement was "tainted" because it involved insiders and would benefit guarantors. The statement was part of the Court's exemplification of Debtor's failure to carry its burden of proof for giving superpriority liens to the insider-creditors. Any other deduction Tri-State Financial has made from that portion of the

decision is at best unfounded rhetoric and at worst ill-conceived bibliomancy.

Contrary to Tri-State Financial's assessment, the Court holds no disdain for the re-engineering project itself. The Court was unwilling to approve the massive project outside the context of a Chapter 11 plan. Unequivocally, the Court also relayed to parties on several occasions its concern the project had proceeded without court approval although Debtor remained in Chapter 11. Nonetheless, the Court also recognized the value of the project itself. At the July 28, 2004, hearing during its findings and conclusions regarding conversion of the case to Chapter 7, the Court stated:

> It would appear that the Chapter 7 Trustee may be able to get the plan[t] up and running within a relatively short period of time or offer the plant for sale, also within a relatively short period of time. They may be able to employee [sic] ICM if that's appropriate and move for credit to complete the upgrade project, again if that's appropriate.

TRANSCRIPT OF RECORD at 91, *In re Tri-State Ethanol Company LLC*, Bankr. No. 03-10194 (July 28, 2004) (file doc. 1322) (bracketed notes correct transcriptionist errors).

Basis No. 3

Tri-State Financial stated recusal is warranted because "the pattern of [the Court]'s rulings . . . have

given every appearance of being improperly vindictive, punitive or both." It surmised the decision to convert the case to Chapter 7 was targeted at Debtor, Tri-State Financial, and the Omaha group and was

> vindictive or punitive mainly for what [the Court] had decided was disregard of his judicial authority, but also perhaps for what he had decided was a scheme and also perhaps, as suggested by the Larsen affidavit, to put or keep Strasheim in his place. This is a more likely explanation than his discussion on July 28, 2004, of Chapter 11 confirmation standards.

Motion for Recusal, ¶ 4.20, Tri-State Financial, L.L.C. (June 29, 2006) (file doc. 1873). It also surmised this punishment may have sprung from Tri-State Financial's failure to consummate a settlement with North Central that was recited on the record June 21, 2004.

On July 27, 2004, when North Central's motion to approve its agreement with Debtor and Tri-State Financial was on the table, the Court confirmed with counsel – several times – that the oral agreement North Central, Debtor, and Tri-State Financial recited on the record June 21, 2004, had not included any provision that it was conditioned on confirmation of a plan. Tri-State Financial's statement that the Court attempted that day "to influence [Tri-State Financial] to agree to pay $1 million for equity while not disclosing to all parties that [Debtor's] Chapter 11 plan could not be confirmed" is inaccurate and erroneously assumed the Court had a significant

understanding of the implications of the parties' June 21, 2004, deal as it related to either North Central or Tri-State Ethanol (the Court was focused on the implications of the settlement as it related to Debtor). At the July 27, 2004, hearing, the Court stated it could not force Tri-State Financial to settle with North Central, and the Court denied North Central's motion requesting approval of that settlement, which was the disposition Tri-State Financial had sought that day. Further, the Court's statements on July 27, 2004, regarding the confirmability of Debtor's proposed plan were to advise the parties what matters would be at issue at the next day's confirmation hearing, nothing more.

At the hearing on July 28, 2004, the Court's statements about the confirmability of Debtor's plan, especially as to feasibility, were a part of its findings and conclusions regarding its decision to convert the case to Chapter 7. The ultimate failure of Debtor, Tri-State Financial, and North Central's June 21, 2004, settlement may have played a role in Debtor's decision not to go forward with confirmation of a plan on July 28, 2004, and to consent to dismissal of the case; the failure of the parties' June 21, 2004, deal, however, was not a material factor in the Court's decision to convert the case to Chapter 7 rather than dismiss it.

In this section of its recusal motion, Tri-State Financial referenced other paragraphs in the motion and thus provided a lengthy discourse on why it had surmised the Court punished Tri-State Financial or

ICM for re-engineering the ethanol plant without court authority and forced it to settle with Trustee Lovald. It says the Court held a hearing on March 2, 2005, to decide whether Trustee Lovald's objection to Tri-State Financial's administrative expense claim "should be sustained without an evidentiary hearing." It also stated the Court had prematurely concluded in its December 12, 2003, decision denying Debtor's Motion to Approve Re-engineering Stipulation that Tri-State Financial was precluded from receiving any administrative expense claim.

Tri-State Financial has reached an overblown conclusion about the purpose of the March 2, 2005, hearing. The initial hearing on Tri-State Financial's administrative expense claim was specifically set as a telephonic hearing, which the Court frequently conducts. The scheduling order for a telephonic hearing on a contested matter, including this one, advises parties an evidentiary hearing will be set, if needed. What actually happened during the March 2, 2005, hearing is set forth in the Court's March 14, 2005, letter decision:

> A telephonic hearing was held March 2, 2005. Tri-State Financial first argued that North Central did not have standing to object. North Central defended saying its position as an equity security holder could be eroded by any payments made to Tri-State Financial on these loan claims. Tri-State Financial countered that since only Debtor would receive any estate residual, only

Debtor, not its shareholders, had standing to protect that potential recovery.

Tri-State Financial next requested an evidentiary hearing on its administrative expense claim. Facts Tri-State Financial claimed were in dispute included whether the unsecured loans for operating expenses were made in the ordinary course of Debtor's business and thus did not need court approval under 11 U.S.C. § 364(a) and whether the loans for equipment purchases constituted a substantial contribution to the estate for which the estate must compensate Tri-State Financial. It argued that since the loans benefitted Debtor and enhanced the sale of the ethanol plant, the estate should not reap a windfall of almost $2,000,000.00 while Tri-State Financial was punished in the same amount for failing to obtain court approval. Finally, Tri-State Financial argued Trustee Lovald should commence an adversary proceeding under Fed.R.Bankr.P. 7001(8) if he wanted Tri-State Financial's loan claim subordinated.

Counsel for Trustee Lovald restated the trustee's position that Tri-State Financial did not hold an administrative claim. He argued that by financially supporting Debtor through unauthorized loans, Tri-State Financial instead had made an equity contribution.

In re Tri-State Ethanol L.L.C., Bankr. No. 03-10194, slip op. at 7 (Bankr. D.S.D. March 14, 2005). The

findings and conclusions the Court made in that interim decision are also best considered from reading the actual decision, not from Tri-State Financial's recollections in its recusal motion.

> *Discussion – standing of North Central Construction.* A Chapter 7 debtor has standing to object only if the contested matter might produce or affect any surplus in the bankruptcy estate that would be returned to the debtor. *Nangle v. Surratt-States (In re Nangle)*, 288 B.R. 213, 215-16 (B.A.P. 8th Cir. 2003) (a Chapter 7 debtor holds a pecuniary interest and may object to a proposed settlement if there is a reasonable possibility of a surplus after all estate debts are paid). A shareholder of a Chapter 7 debtor-corporation, however, does not enjoy the same standing. Generally, an action to enforce corporate rights or redress injuries to a corporation may not be maintained by a shareholder in his own name, even though the perceived injury to the corporation may result in a decline in the value of the stock. *Sinclair v. Hawke*, 314 F.3d 934, 939 (8th Cir. 2003) (cites therein).
>
> The Bankruptcy Appellate Panel in this Circuit has held that a shareholder of a Chapter 7 debtor would have standing to object to a proposed settlement by the case trustee if the shareholder could establish that a successful objection would result in an estate surplus. *Yates v. Forker (In re Patriot Co.)*, 303 B.R. 811, 815 (B.A.P. 8th Cir. 2003). While the decision acknowledged that the

objector was the *sole* shareholder of the debtor, the Court's conclusion did not appear to hinge on that fact. In light of *Sinclair*, 314 F.3d at 939, however, that distinction undoubtedly remains important. *See, e.g., Freishtat v. Blair (In re Blair)*, 319 B.R. 420, 436 (Bankr. D. Md. 2005) (sole shareholder had standing to object to fee application where its outcome would affect her pecuniary interest).

Accordingly, the Court concludes that North Central does not have standing, as an equity holder in Debtor, to object to Tri-State Financial's administrative expense claim against the bankruptcy estate. Moreover, as long as sufficient funds have been placed in escrow to pay North Central's non equity claim in full, North Central also does not have standing to object as an estate creditor. North Central will, therefore, need to look to Debtor to protect any potential estate surplus from improper or exaggerated claims.

Discussion – necessity of an evidentiary hearing on Tri-State Financial's administrative expense claim. A Chapter 11 debtor-in-possession may incur unsecured post-petition debt without court-approval if the debt is incurred in the ordinary course of business and if the debt constitutes an administrative expense under § 503(b)(1). 11 U.S.C. §§ 364(a), 1107, and 1108. Two tests are usually employed when determining whether unsecured credit is being incurred in the ordinary course of business. *In re Blessing Industries,*

Inc., 263 B.R. 268, 272 (Bankr. N.D. Iowa 2001) (cites therein). The *vertical* test is whether a reasonable creditor would view the transaction as deviating from the debtor's normal day-to-day operations. *Id.*

> If the transaction is something that might be considered "unusual, controversial or questionable" the creditors have a right to be notified so that they have an opportunity to object.

Id. (quoting *In re Husting Land & Dev., Inc.*, 255 B.R. 772, 779 (Bankr. D. Utah 2000)). The horizontal test considers whether the credit transaction falls within a range of accepted practices within the debtor's particular industry. *Blessing Industries*, 263 B.R. at 272 (cites therein).

For the unsecured debt to be an administrative expense under § 503(b)(1), it must represent "actual, necessary costs and expenses of preserving the estate," a provision which courts generally have construed narrowly. *AgriProcessors, Inc. v. Iowa Quality Beef Supply Network, L.L.C. (In re Tama Beef Packing, Inc.)*, 290 B.R. 90, 96 (B.A.P. 8th Cir. 2003). Two questions need to be answered. First, did the expense arise from a transaction with the bankruptcy estate? *Id.* Second, did the transaction benefit the estate in some demonstrable way? *Id.*

The claimant must show that *other* unsecured creditors received tangible benefits

> from the services or goods provided by the claimant. *In re Jack Winter Apparel, Inc.*, 119 B.R. 629, 633 (E.D. Wisc. 1990); *Kinnan & Kinnan Partnership v. Agristor Leasing*, 116 B.R. 162, 166 (D. Neb. 1990); *In re Herrick*, Bankr. No. 184-00041, slip op. at 2 (Bankr. D.S.D. May 9, 1988). Incidental benefit to the estate or extensive participation in the case, standing alone, is not a sufficient base for an administrative [expense] status. *Jack Winter Apparel, Inc.*, 119 B.R. at 633. A creditor's efforts undertaken solely to further its own self-interest [are] not compensable. *Id.*
>
> *In re Bellman Farms, Inc.*, 140 B.R. 986, 995 (Bankr. D.S.D. 1991). The claimant's burden is by a preponderance of evidence. *Id.*; *In re Bridge Information Systems, Inc.*, 288 B.R. 133, 137-38 (Bankr. E.D. Mo. 2001); and *In re Hanson Industries, Inc.*, 90 B.R. 405, 409 (Bankr. D. Minn. 1988).
>
> Tri-State Financial undoubtedly will have a difficult time establishing that the subject loans it made to Debtor during the Chapter 11 administration were made in the ordinary course of Debtor's business, especially where Debtor sought court approval for other loans for the same or similar purposes. Nonetheless, the Court will give Tri-State Financial an opportunity to make that showing.

In re Tri-State Ethanol L.L.C., Bankr. No. 03-10194, slip op. at 7-10 (Bankr. D.S.D. March 14, 2005). While

Tri-State Financial considers the interim decision as implicit evidence the Court had pre-judged its administrative expense claim, the decision demonstrates otherwise. The Court reviewed the applicable law and the facts of record. While the Court set forth the legal burdens Tri-State Financial faced and also forewarned Tri-State Financial it had a difficult road to travel based on the present law and fact, the Court did not foreclose the administrative claim. Tri-State Financial again misstated the record when it alleged

> without warning or request, on March 23, 2005, [the Court] sua sponte entered an order shortening the time for [Tri-State Financial] to file its answer to April 8, 2005, fixing April 22, 2005, as the deadline to complete discovery and scheduling a trial on May 2, 2005, thereby arbitrarily depriving [Tri-State Financial] of the benefits of the Federal Rules of Bankruptcy Procedure for adversary proceedings. Later he denied [Tri-State Financial]'s request for a continuance.

Motion for Recusal, ¶ 4.33, Tri-State Financial, L.L.C. (June 29, 2006) (file doc. 1873). The Court advised the parties in the March 14, 2005, interim decision that all matters regarding Tri-State Financial's claim would be heard together:

> The Court, however, is not going to hold successive hearings on Tri-State Financial's alternative theories of recovery and the objections thereto. Consequently, any objection to Tri-State Financial's alternative theory that it holds a general unsecured claim for

> repayment of these loans [footnote omitted] should be filed promptly, and any adversary proceeding by Trustee Lovald or another party in interest that Tri-State Financial's claim should be subordinated under 11 U.S.C. § 510© [sic] and Fed.R.Bankr.P. 7001(8) should be commenced promptly. A combined evidentiary hearing/trial date will then be set by separate order.

In re Tri-State Ethanol L.L.C., Bankr. No. 03-10194, slip op. at 10 (Bankr. D.S.D. March 14, 2005). That the answer period in the adversary proceeding had to be shortened to accomplish that directive was obvious. Tri-State Financial's subsequent motion to reschedule and extend certain deadlines was denied because, as related above, the Court had earlier advised counsel that all matters related to Tri-State Financial's claim would be heard together and because alternative court dates were not readily available. What Tri-State Financial also failed to recall in its recusal motion is its second motion to reschedule *was* granted after some unavoidable discovery problems arose and a date on the Court's calendar became available.

Tri-State Financial has also concluded the Court forced it to settle with Trustee Lovald and the Court somehow dictates Trustee Lovald's decisions regarding the claims to which he will object. Both conclusions defy the record and inappropriately castigate the Court's and Trustee Lovald's professionalism and character. If anything has encouraged settlements in

this case – and should continue to encourage them – it is the fact that the estate has sufficient funds to pay all or nearly all claims and the fact that litigating the construction-related disputes would be horrendously expensive and time-consuming.

As to which claims Trustee Lovald files objections, the Court simply has no knowledge of the disputed claims or the grounds for those disputes until Trustee Lovald files his objections. That Reporter Larsen surmised otherwise demonstrates an ignorance, in general, of the Court's actual relationship with all case trustees and, in particular, of the statutory duty Trustee Lovald has to investigate each of the many claims in this case and litigate those that are objectionable.

Similar to its allegations regarding the Court's treatment of John Hoich, James Jandrain, and Attorney Strasheim, which are discussed above, Tri-State Financial claimed this Court punished Randy Kramer for being a member of the Omaha Group by reducing his claim. As noted above, Randy Kramer did not file a claim in this case. As also discussed above, the claim held by Western Biomass, the corporation of which Kramer owns half the stock, was reduced because there was no record Debtor had agreed to pay that company a $17,500.00 bonus. There was no punishment; there simply was no evidence to support that portion of Western Biomass' claim. Tri-State Ethanol also argued the Court has not applied that

same standard to other creditors' claims. It has, to James Jandrain's.[21] No other claims of a similar nature have yet come before the Court.

Finally, under this third "Basis for Bias," Tri-State Financial said the Court "appears to have decided that as punishment there should be no return to holders of equity interests in [Debtor.]" It reaches this conclusion based on the Court's "withholding of any rulings on [Tri-State Financial]'s objections to claims and by his rulings on appointment of professionals and allowance of their fees."

As discussed by Trustee Lovald in his response and affidavit regarding Tri-State Financial's recusal motion, there has never been any legitimate expectation equity holders would receive a significant return on their investments in this case. Moreover, contrary to Tri-State Financial's contentions, that reality is not a product of this Court's action.

Tri-State Financial's allegations regarding the Court's orders on the appointment and compensation of professionals is discussed below.

Basis No. 4

Tri-State Financial claimed a "fully informed average person on the street might also reasonably

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[21] In this section, Tri-State Financial repeated its charges that the Court punished James Jandrain by denying his claim. Those charges are discussed above.

doubt [the Court]'s impartiality based on a pattern of prejudgments, discriminatory, and unfair treatment of [Tri-State Financial] as compared to other litigants in the case." It again offered as evidence its allegations that the Court blamed Tri-State Financial when it, Debtor, and North Central failed to consummate the deal they reported on the record June 21, 2004. As discussed above, the only thing the Court confirmed with counsel in Chambers and during the July 27, 2004, hearing was that the parties had not stated on the record June 21, 2004, that confirmation of Debtor's pending Chapter 11 plan was a condition of the agreement. Moreover, the June 21, 2004, agreement was never approved and is no longer at issue.

Tri-State Financial offered the in-court auction of the ethanol plant as additional evidence the Court has favored other parties over it. Trustee Lovald's July 20, 2006, affidavit lays that allegation to rest. As he recites, any changes to the sale terms and conditions made on the sale day were by mutual consent of all the parties involved. For Tri-State Financial to make charges to the contrary is reckless. *See* S.D.C.L. ch. 16-18, appendix, Rule 3.3, SOUTH DAKOTA RULES OF PROFESSIONAL CONDUCT; *Midwest Motor Sports v. Arctic Sales, Inc.*, 347 F.3d 693, 697-98 (8th Cir. 2003) (South Dakota's Rules applied in matter before federal district court). That Reporter Larsen, who is not law trained, left the sale hearing with misconceptions and an incomplete comprehension of what had taken place is understandable. Any changes to the sale terms and conditions made that day, however, were

done only with the consent of all interested parties. Further, the changes benefitted the estate, and thus creditors, by insuring the best sale price and sale terms were obtained. Moreover, no appeal or motion to alter or amend the sale order was timely filed. Tri-State Financial was the ultimate purchaser when the original bidder could not close timely, and Tri-State Financial's back up bid became the successful bid.

It is true the Court denied an earlier motion by Tri-State Financial to change some of the sale terms. That motion, which was filed *after* a contested motion to set sale terms had been resolved, requested substantial changes Tri-State Financial could and should have requested when the sale terms motion was pending. In an October 8, 2004, letter decision denying Tri-State Financial's motion to amend the same terms order, the Court thoroughly addressed Tri-State Financial's four concerns. To allude the sale term changes Tri-State Financial wanted through that motion and the sale term changes that were made by mutual consent on the sale day were essentially the same and were only granted because some other party requested them is an oversimplification – if not misstatement – of the record by Tri-State Financial.

Under this fourth "Basis for Bias," Tri-State Financial repeated its allegation that in March 2005 the Court pre-judged its administrative expense claim, shortened the answer time in the related adversary proceeding commenced by Trustee Lovald, and denied its motion to delay the hearings on its

claim and the related adversary proceeding. Those allegations are addressed above, including those portions of the record Tri-State Financial has misinterpreted or simply ignored. In this section of its recusal motion, however, Tri-State Financial relied on these allegations for its conclusion that the Court has become a "virtual advocate against [Tri-State Financial]." It also added two more allegations:

> In considering whether to confirm [Debtor]'s modified plan of Reorganization, Judge Hoyt invoked his duty to independently apply confirmation standards [and i]n considering attorneys fees for the Trustee and creditors, [the Court] does not invoke his duty to independently pass on such fees. In both cases, there is likely injury to [Tri-State Financial] which is known to [the Court].

Motion for Recusal, ¶ 4.34, by Tri-State Financial, L.L.C. (June 29, 2006) (file doc. 1873).

Tri-State Financial has again misstated the record. A confirmation hearing was never held in this case so no objections of any nature were ever formally considered. Objections to confirmation by North Central were still on the table for the evidentiary confirmation hearing set for July 28, 2004. When the confirmation hearing was called as the first matter on the calendar that day, Debtor announced it was consenting to dismissal of the case.

As to the Court's rulings on professional's fee applications, the Court identified fifteen fee applications that have come before it in this case to date. Five of those have been contested. One, an application by Debtor's original counsel and his firm, was withdrawn. One application by special counsel for the estate was approved with modifications made at the request of the United States Trustee. In another, filed by a creditor's attorney, the United States Trustee withdrew its objection. Creditor First Dakota's request for attorneys' fees under § 506(b) was reduced following a hearing, and the order is still subject to a motion to amend. The fifth, by one of the estate's special counsel, has yet to be set for hearing.

Of the ten uncontested fee applications, no objections were filed, and the Court found no basis to bring the matters on for hearing *sua sponte*. The Court finds it difficult to understand how Tri-State Financial can castigate the Court for not "objecting" to any of these ten fee applications when Tri-State Financial itself did not file objections to any of them.

Tri-State Financial made similar allegations regarding applications to employ estate professionals and conflict of interest issues. It is true Debtor's original out-of-state bankruptcy counsel faced removal due to alleged conflicts of interest created by his and his firm's representation of both Debtor and some equity security holders who had formed Tri-State Financial. The Court, however, never entered a ruling on that matter. The attorney and his firm withdrew from continued representation of Debtor

and withdrew their fee application. One of the estate's attorneys, Robert E. Hayes, is presently facing conflict of interest charges by Tri-State Financial, which were made as part of its objection to his fee application. That matter has not yet been set for hearing. The Court knows of no other similar employment or conflict of interest issues.

Tri-State Financial claimed the Court has Trustee Lovald under his "control and [Trustee Lovald is] not independent." In this portion of its motion, Tri-State Financial offered as evidence the fact Trustee Lovald changed his position on whether the parties had reached a settlement following the mediation with Judge Simko, and it alleged the Court became a "virtual advocate" for North Central at the May 4, 2006, hearing on Trustee Lovald's motion to approve the mediated settlement.

Tri-State Financial's allegations are again overstated. It is undisputed Trustee Lovald initially took the position the parties' mediated settlement with Judge Simko could not be presented by him for approval by the Bankruptcy Court. Trustee Lovald, however, in his objection to North Central's motion, acknowledged "core agreements" had been reached that day. He also identified an indemnity issue as the major stumbling block that had prevented the completion of a written agreement. At the February 9, 2006, hearing, Tri-State Financial also agreed some "core agreements" had been reached in the mediation. Based on that record, the Court concluded the core agreements constituted a stipulation Trustee Lovald

could notice for objections. The Court further concluded the transcript of the settlement report the parties made before Judge Simko after the mediation was the best evidence of what constituted the core agreements. That Trustee Lovald then advocated in support of approval of the "core agreements" in a subsequent motion was legally prudent and consistent with the record on February 9, 2006. Moreover, Trustee Lovald's motion to approve the mediated settlement was later denied. The Court, thus, could not have then "pre-judged" the trustee's motion. Moreover, the Court gave North Central little input at the May 4, 2006, hearing on the trustee's settlement motion because North Central did not have a pleading on the table.

In this portion of the recusal motion, Tri-State Financial also stated:

> On July 7, 2005, counsel for the Trustee had filed a motion for leave to make Gaylor Engineering a party to the Trustee's litigation in [North Central]'s claim. The logical reason for this is that Gaylor Engineering and [North Central] can be expected to point the finger at each other for defective engineering and defective construction as the party to blame for the Ethanol Plant not working as it was supposed to work. On the same day, Judge Hoyt sua sponte denied the Trustee's Motion.

Motion for Recusal, ¶ 4.37, by Tri-State Financial, L.L.C. (June 29, 2006) (file doc. 1873). Though it is

unclear, apparently Tri-State Financial believed the Court's denial of this motion was intended to favor another party and punish it. As the Court stated in its ruling on the trustee's motion to bring Gaylor Engineering into an adversary on a third party complaint, the motion was untimely, and the existing adversary did not lend itself to a third-party complaint against Gaylor Engineering. The denial was without prejudice to a subsequent contested matter or adversary proceeding regarding Gaylor Engineering's claim. In fact, such an adversary proceeding was commenced by Trustee Lovald against Gaylor Engineering while this recusal motion was under advisement.

Basis No. 5

Tri-State Financial contended the Court "at times appears to have aligned himself with [North Central] and in favor of [North Central]. It charged the Court has "yet to question the enforceability, validity or amount of the Claim of [North Central] or [North Central]'s motives in opposing [Debtor] and [Tri-State Financial] every step of the way." It further claimed the Court has "indulged" North Central "in nearly all its tactics of questionable motivation."

It is true the Court has not yet ruled on North Central's claim. Trustee Lovald's and Tri-State Financial's respective objections to North Central's claim have not yet been heard. The parties' interceding attempts to achieve a global settlement have

delayed resolution, not the Court. Further, Trustee Lovald has now reached a settlement with North Central, and that settlement, to which Tri-State Financial has objected, is ready to be set for hearing. If the trustee's settlement is not approved, then Trustee Lovald's and Tri-State Financial's objections to North Central's claim will be on the table, along with the attendant July 8, 2005, discovery-related motion and the June 21, 2006, "intervention" motion Tri-State Financial has filed.[22]

Because North Central's claim has not yet come before the Court, the Court is not conversant about what is encompassed in North Central's claim or the objections to it. Why Tri-State Financial thinks the

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[22] Because it has a pecuniary interest in any proposed settlement of North Central's claim, Tri-State Financial has standing to object to any proposed compromise of North Central's claim, as well as to object to the claim itself. *See White v. Coors Distributing Co. (In re White)*, 260 B.R. 870, 875 (B.A.P. 8th Cir. 2001) (party with pecuniary interest may object to a claim). At times, however, it appears Tri-State Financial and its counsel do not acknowledge Trustee Lovald has the authority to compromise North Central's claim, subject to court approval, and that any proposed settlement of the claim should be considered *before* extensive discovery or litigation regarding the objections to North Central's claim. *See* 11 U.S.C. § 704; Fed.R.Bankr.P. 9019; *Martin v. Cox (In re Martin)*, 212 B.R. 316, 319 (B.A.P. 8th Cir. 1997). Were it not so, the estate would be deprived of some of the cost and time-saving benefits of a compromise. *Id.*; *ReGen Capital III, Inc. v. Official Committee of Unsecured Creditors (In re Trism, Inc.)*, 282 B.R. 662, 668 (B.A.P. 8th Cir. 2002) ("A major purpose of compromise is to avoid the expense, burdens, and uncertainty associated with litigation. [Cite omitted.]").

Court should already be aware of that information, *see* ¶ 4.41 of its recusal motion, is in direct opposition to its several contentions the Court should not prejudge matters.

Tri-State Financial also claimed the Court

> has appeared to favor [North Central] procedurally by such things as the scheduling a trial date to decide objections to [North Central]'s claim that make it impossible for the Trustee and [Tri-State Financial] to adequately prepare for trial and other similar actions, by unnecessarily scheduling hearings at geographically distant places, and by not ruling, at the Trustee's request, and disputes in which the Trustee and [Tri-State Financial] are adversaries.

Motion for Recusal, ¶ 4.42, Tri-State Financial, L.L.C. (June 29, 2006) (file doc. 1873). As noted above, the original evidentiary hearing on North Central's claim, scheduled for August 29, 2005, was set by order entered June 10, 2005. Consequently, the parties had more than two months to prepare. Further, the August 29, 2005, evidentiary hearing was put on hold at the parties' request due to their mediated settlement with Judge Simko.

As to holding hearings at "geographically distant places," the divisional courthouse for this case is in Aberdeen, South Dakota. Only one active attorney is from that area. The attorneys for the other active parties are mostly from southeastern South Dakota, one is from Omaha, Nebraska, and another is from

Minneapolis, Minnesota. The most convenient place for hearings has, thus far, been Sioux Falls, South Dakota. The Court's records indicate all but four hearings have been held there. Four hearings have been held in Pierre, South Dakota – two in 2003 and two in 2004 – where the undersigned has his chambers and a more readily available courtroom. Accordingly, the basis for Tri-State Financial's complaints in this regard are unfounded.

Though it is not entirely clear from this portion of the recusal motion, Tri-State Financial also seems to contend the Court has delayed rulings, at Trustee Lovald's request, on matters of dispute between Trustee Lovald and Tri-State Financial. The Court does not know what those matters are, and it has not delayed any rulings at Trustee Lovald's behest.

Basis No. 6

Tri-State Financial's final grounds for recusal is that it believes the Court has been too involved in the parties' various settlement attempts and has become privy to the specifics of those negotiations, in large part because of North Central's November 18, 2005, letter to the Court, and the Court's statements regarding the settlement Debtor, North Central, and Tri-State Financial reported on the record June 21, 2004.

Contrary to Tri-State Financial's assertions, the Court has not taken an active role in the settlements. It has virtually no knowledge of the "offers, amounts,

and the like" as Tri-State Financial believes. To the extent it could have gleaned a portion of that information by studying North Central's November 18, 2005, letter to the Court and the several attachments thereto, the Court has not done so. The letter was not appropriately sent by North Central, a fact on which the Court has always agreed with Tri-State Financial and a fact the Court tried to convey to North Central at the telephonic hearing on November 18, 2005. Moreover, one of the attachments with which Tri-State Financial takes issue – the transcript of the mediation settlement report – was subsequently determined on February 9, 2006, not to be privileged, since it essentially contained only the results of the mediation, not the exchanges that lead to it.

To the extent the parties have disclosed offers and counteroffers in subsequent hearings or pleadings, the Court has not requested they do so, and any such disclosures, which have been minimal, have not been material to any of the Court's decisions to date. They will also not be material in any subsequent decision.

As to the Court's statements regarding the settlement among Debtor, Tri-State Financial, and North Central that was reported on the record June 21, 2004, the Court only reiterated on July 27, 2005, that confirmation was never stated on June 21, 2004, to be a condition of the agreement. The Court did not have a detailed understanding of the impact the

agreement would have on the two creditors involved but instead focused on the impact the agreement would have on the bankruptcy estate.

Tri-State Financial has relied upon *United States v. Pfizer, Inc.*, 560 F.2d 319 (8th Cir. 1977). In *Pfizer*, the appellate court found the trial court had "participated in settlement negotiations to an extraordinary degree" and had

> continued to play an active and aggressive role in settlement negotiations, expressing strong opinions on the merits of the case and expressing his monetary evaluation of [one party]'s claims against these appellants. . . ."

Id. at 322. That Tri-State Financial somehow equates this Court's actions in this case with those of the trial court in *Pfizer* is a gross exaggeration of the record. In contrast to the facts in *Pfizer*, the Court here knows only the results of settlements that have been reported on the record, including the record made before Judge Simko. The Court is not privy to the intricate legal give and take the parties have endured in their settlement attempts, nor does it want to be privy to it.

In this portion of its recusal motion, Tri-State Financial again expressed disdain for the Court's alleged lack of

> concern that [Tri-State Financial] would pay $1 million for equity in a Chapter 7 case and $1.5 million for a disputed claim. This was so even though Judge Hoyt knew on November

> 18, 2005, that [North Central], shortly after July 29, 2004, had filed a lawsuit against [Tri-State Financial] seeking to enforce the purported settlement but had done virtually nothing to get the case to progress to trial for two years.

Motion for Recusal, ¶ 4.49 (in pertinent part), by Tri-State Financial, L.L.C. (June 29, 2006) (file doc. 1873). This Court has no recollection of when it learned North Central had filed suit against Tri-State Financial in federal district court, has never seen the pleadings for that action, and, obviously, has no ability to make that suit "progress to trial." If Tri-State Financial was referring to the fact North Central's claim has not yet been considered at a bankruptcy court hearing, that delay, as discussed above, has been the product of the parties' attempted settlements, not the Court's actions.

Contrary to Tri-State Financial's assertions in paragraph 4.52 of its recusal motion, the Court does not believe it is the only bankruptcy judge who can resolve the remaining disputes in this case. The undersigned's decision to delay his retirement to finish the case only arises from a sense of duty and an awareness that a change of judge will further delay administration, not any concept that his familiarity with the parties is a necessary component of addressing the remaining disputes.

Application of § 455(a)

As discussed above, under § 455(a) the Court must objectively consider whether his impartiality might reasonably be questioned by the average person on the street who knows all the relevant facts of a case. The Court stands on the record and writings and concludes an average person would *not* question his impartiality in this case.

For an average person to comprehend all the relevant facts in this case would be a notable accomplishment. Even the Court's necessary regurgitation in this decision of what has transpired to date has been an arduous, time-consuming task. However, the Court is confident, once that comprehension existed, an average person would understand this has been a difficult case, two of the parties have been at loggerheads since before the bankruptcy case began and are still so today, and resolution of some remaining claims and related issues will not be easy. The average person would also find the Court on several occasions has been short with counsel for all parties, especially counsel for Tri-State Financial, who often rehashes issues and arguments that have previously been addressed, and who sometimes encumbers his pleadings and arguments with side issues and comments not relevant to the matter at hand. Fully cognizant of all the facts, however, the average person would share the Court's frustrations with the unnecessary roadblocks and detours in the administration of this case and, at least to some extent, would empathize with his sometimes brusk demeanor.

The average person would note nearly all, if not all, the major players in this case have had court decisions go both in their favor and against them; Tri-State Financial is no exception. The average person, cognizant of all facts, would conclude Tri-State Financial has not been singled out for abuse, nor have others been given a halo by the Court. The average person on the street, fully aware of what has happened in this case, would not question the Court's impartiality. Accordingly, the Court will not recuse itself under 28 U.S.C. § 455(a).

Application of § 455(b)(1)

As discussed in part II above, the undersigned should recuse himself under § 455(b)(1) if he holds an actual bias for or against one of the parties. Despite Tri-State Financial's voluminous allegations to the contrary, the Court does not hold any such bias, let alone a deep-seated and pervasive one that would dictate recusal.

After more than 30 years as a trial court judge, including over 18 years as a Bankruptcy Court judge, the undersigned has found this case to be one of the more difficult ones over which he has presided, not because of its legal complexity but due to the sheer volume of contested matters and the animosity among major parties. That difficulty also makes the case more interesting and a greater challenge to govern; it does not by necessity foster or result in any bias for or against any party or their counsel.

Obviously, due to the voluminous pleadings and numerous hearings and conferences over a handful of years, the Court has formed opinions about the parties and their counsel. Those opinions have arisen only from the record before it. The Court has no extra-judicial knowledge of the case or the litigants. Moreover, the judicial opinions the Court has formed do not include any deep-seated or pervasive bias for or against any party. To the extent Tri-State Financial and its counsel are convinced otherwise, they are only doing themselves and the other litigants a great disfavor.

Since no actual bias exists and since the Court is confident it can continue to provide a fair tribunal, Tri-State Financial's request for recusal under § 455(b)(1) will be denied.

Application of the Due Process Clause

Tri-State Financial also sought recusal under the "[t]he Due Process Clause(s) of the United States Constitution in the Fifth and Fourteenth Amendments[, which] guarantee to [Tri-State Financial] the right to trial before an objective, impartial, and fair tribunal and the appearance of an objective, impartial, and fair tribunal." It claims if the undersigned were to conduct any trial on which Tri-State Financial is a party or has an interest, Tri-State Financial would be deprived of due process.

The Fourteenth Amendment provides in relevant part that no state "shall deprive any person of life, liberty, or property without due process of law[.]" It is textually identical to the due process clause in the Fifth Amendment, which provides, in relevant part, that a person shall not "be deprived of life, liberty, or property without due process of law[.] *Carhart v. Gonzales*, 413 F.3d 791, 795 n.2 (8th Cir. 2005). While the Fourteenth Amendment applies to states, not this federal tribunal, the Fifth Amendment's Due Process Clause "has a broader reach" and applies to the federal government, *id.*, including this Court.

> A fair trial in a fair tribunal is a basic requirement of due process. Fairness of course requires an absence of actual bias in the trial of cases. But our system of law has always endeavored to prevent even the probability of unfairness. To this end no man can be a judge in his own case and no man is permitted to try cases where he has an interest in the outcome. That interest cannot be defined with precision. Circumstances and relationships must be considered. This Court has said, however, that 'Every procedure which would offer a possible temptation to the average man as a judge * * * not to hold the balance nice, clear, and true between the State and the accused denies the latter due process of law.' *Tumey v. State of Ohio*, 273 U.S. 510, 532, 47 S.Ct. 437, 444, 71 L.Ed. 749. Such a stringent rule may sometimes bar trial by judges who have no actual bias and who would do their very best to weigh

> the scales of justice equally between contending parties. But to perform its high function in the best way 'justice must satisfy the appearance of justice.' *Offutt v. United States*, 348 U.S. 11, 14, 75 S.Ct. 11, 13.

In re Murchison, 349 U.S. 133, 136 (1955).

This standard is, obviously, quite high. However, since Tri-State Financial's claim for recusal under § 455 failed to "pass muster," the claim also "cannot survive the more rigorous standards required of [such a] claim under the due process clause." *Sypolt*, 346 F.3d at 840; *Larsen*, 427 F.3d at 1095. Therefore, Tri-State Financial's request for recusal under the Fifth Amendment's Due Process Clause will be denied.

Timeliness of the Motion for Recusal

As to the timeliness of Tri-State Financial's recusal motion, Trustee Lovald is correct that Tri-State Financial could have brought the motion sooner, especially since Tri-State Financial first intimated on the record the undersigned was being unfair at the November 18, 2005, telephonic hearing. *See, e.g., In re Kansas Public Employees Retirement System*, 85 F.3d 1353, 1360 (8th Cir. 1996); *Oglala Sioux Tribe v. Homestake Mining Co.*, 722 F.2d 1407, 1414 (8th Cir. 1983). Therefore, the motion is also denied as being untimely.

Having concluded that recusal under 28 U.S.C. §§ 455(a) or (b)(1) or the Due Process Clause of the Fifth Amendment is not warranted and that the

motion was untimely, Tri-State Financial's *Motion for Recusal* will be denied. An appropriate order will be entered. The Court will enter decisions on the matters already under advisement as quickly as possible. Scheduling orders on pending contested matters will be entered soon.

Dated this 1st day of September, 2006.

BY THE COURT:

/s/ Irvin N. Hoyt
Irvin N. Hoyt
Bankruptcy Judge

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 07-2430

Tri-State Financial, LLC,

Appellant

v.

John S. Lovald and Murphy Brothers,

Appellees

No: 07-2433

Tri-State Financial, LLC,

Appellant

v.

Robert E. Hayes and Davenport,
Evans, Hurwitz & Smith,

Appellees

Appeal from U.S. District Court
for the District of South Dakota
(1:06-cv-01040-CBK)
(1:07-cv-01003-CBK)

ORDER

The petition for rehearing en banc is denied. The petition for rehearing by the panel is also denied. Judge Wollman did not participate in the consideration or decision of this matter.

June 24, 2008

Order Entered at the Direction of the Court:
Clerk, U.S. Court of Appeals, Eighth Circuit.

/s/ Michael E. Gans

U.S. CONST. ART. V

ARTICLE [V.]

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

28 U.S.C. § 455. Disqualification of justice, judge, or magistrate judge

(a) Any justice, judge, or magistrate judge of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.

(b) He shall also disqualify himself in the following circumstances:

(1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding;

(2) Where in private practice he served as lawyer in the matter in controversy, or a lawyer with whom he previously practiced law served during such association as a lawyer concerning the matter, or the judge or such lawyer has been a material witness concerning it;

(3) Where he has served in governmental employment and in such capacity participated as counsel, adviser or material witness concerning the proceeding or expressed an opinion concerning the merits of the particular case in controversy;

(4) He knows that he, individually or as a fiduciary, or his spouse or minor child residing in his household, has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceeding;

(5) He or his spouse, or a person within the third degree of relationship to either of them, or the spouse of such a person:

(i) Is a party to the proceeding, or an officer, director, or trustee of a party;

(ii) Is acting as a lawyer in the proceeding;

(iii) Is known by the judge to have an interest that could be substantially affected by the outcome of the proceeding;

(iv) Is to the judge's knowledge likely to be a material witness in the proceeding.

(c) A judge should inform himself about his personal and fiduciary financial interests, and make a reasonable effort to inform himself about the personal financial interests of his spouse and minor children residing in his household.

(d) For the purposes of this section the following words or phrases shall have the meaning indicated:

(1) "proceeding" includes pretrial, trial, appellate review, or other stages of litigation;

(2) the degree of relationship is calculated according to the civil law system;

(3) "fiduciary" includes such relationships as executor, administrator, trustee, and guardian;

(4) "financial interest" means ownership of a legal or equitable interest, however small, or a relationship as director, adviser, or other active participant in the affairs of a party, except that:

(i) Ownership in a mutual or common investment fund that holds securities is not a "financial interest" in such securities unless the judge participates in the management of the fund;

(ii) An office in an educational, religious, charitable, fraternal, or civic organization is not a "financial interest" in securities held by the organization;

(iii) The proprietary interest of a policyholder in a mutual insurance company, of a depositor in a mutual savings association, or a similar proprietary interest, is a "financial interest" in the organization only if the outcome of the proceeding could substantially affect the value of the interest;

(iv) Ownership of government securities is a "financial interest" in the issuer only if the outcome of the proceeding could substantially affect the value of the securities.

(e) No justice, judge, or magistrate judge shall accept from the parties to the proceeding a waiver of any ground for disqualification enumerated in subsection (b). Where the ground for disqualification arises only under subsection (a), waiver may be accepted provided it is preceded by a full disclosure on the record of the basis for disqualification.

(f) Notwithstanding the preceding provisions of this section, if any justice, judge, magistrate judge, or bankruptcy judge to whom a matter has been assigned would be disqualified, after substantial judicial time

has been devoted to the matter, because of the appearance or discovery, after the matter was assigned to him or her, that he or she individually or as a fiduciary, or his or her spouse or minor child residing in his or her household, has a financial interest in a party (other than an interest that could be substantially affected by the outcome), disqualification is not required if the justice, judge, magistrate judge, bankruptcy judge, spouse or minor child, as the case may be, divests himself or herself of the interest that provides the grounds for the disqualification.

CODE OF CONDUCT FOR UNITED STATES JUDGES

CANON 1

A JUDGE SHOULD UPHOLD THE INTEGRITY AND INDEPENDENCE OF THE JUDICIARY

An independent and honorable judiciary is indispensable to justice in our society. A judge should participate in establishing, maintaining, and enforcing high standards of conduct, and should personally observe those standards, so that the integrity and independence of the judiciary may be preserved. The provisions of this Code should be construed and applied to further that objective.

CANON 2

A JUDGE SHOULD AVOID IMPROPRIETY AND THE APPEARANCE OF IMPROPRIETY IN ALL ACTIVITIES

A. A judge should respect and comply with the law and should act at all times in a manner that promotes public confidence in the integrity and impartiality of the judiciary.

CANON 3

A JUDGE SHOULD PERFORM THE DUTIES OF THE OFFICE IMPARTIALLY AND DILIGENTLY

The judicial duties of a judge take precedence over all other activities. In performing the duties prescribed by law, the judge should adhere to the following standards:

A. *Adjudicative Responsibilities.*

* * *

(4) A judge should accord to every person who is legally interested in a proceeding, or the person's lawyer, full right to be heard according to law, and, except as authorized by law, neither initiate nor consider *ex parte* communications on the merits, or procedures affecting the merits, of a pending or impending proceeding. A judge may, however, obtain the advice of a disinterested expert on the law applicable to a proceeding before the judge if the judge gives notice to the parties of the person consulted and the substance of the advice, and affords the parties reasonable opportunity to respond. A judge may, with consent of the parties, confer separately with the parties and their counsel in an effort to mediate or settle pending matters.

* * *

(6) A judge should avoid public comment on the merits of a pending or impending action, requiring similar restraint by court personnel subject to the judge's direction and control. This proscription does

not extend to public statements made in the course of the judge's official duties, to the explanation of court procedures, or to a scholarly presentation made for purposes of legal education.

* * *

C. *Disqualification.*

(1) A judge shall disqualify himself or herself in a proceeding in which the judge's impartiality might reasonably be questioned, including but not limited to instances in which:

(a) the judge has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding;

* * *

IN THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

Tri-State Financial, LLC,

Appellant,

v.

John S. Lovald;
Murphy Brothers,

Appellees (No. 07-2430)

and

Tri-State Financial, LLC,

Appellant,

v.

Robert E. Hayes; Davenport, Evans, Hurwitz & Smith

Appellees (No. 07-2433)

CASE NOS. 07-2430
07-2433

APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF SOUTH DAKOTA

The Honorable Charles B. Kornmann, United States District Judge

PETITION FOR REHEARING EN BANC

Jerrold L. Strasheim
of Baird Holm LLP
1500 Woodmen Tower
Omaha, Nebraska 68102-2068
(402) 344-0500
Attorneys for Appellant

TO THE HONORABLE JUDGES OF THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

Appellant, Tri-State Financial, LLC ("TSF"), pursuant to Fed.R.App.P. 35(b)(1)(A) and 35(b)(1)(B),

and 8th Cir. R. 35A, respectfully presents this Petition for Rehearing En Banc on the panel's decisions that the bankruptcy judge was not required to recuse himself under 28 U.S.C. §455(a) or (b) or both.[1]

FRAP 35(b)(1)(A) STATEMENT: The panel's decision conflicts with the decisions of this Court in: **(1)** *In re Federal Skywalk Cases*, 680 F.2d 1175, 1184 (8th Cir.), *cert. denied*, 459 U.S. 988 (1982) (§455(a) recusal must be evaluated in light of full record) ("*Skywalk*"); **(2)** *Moran v. Clarke*, 296 F.3d 638, 649 (8th Cir. 2002) (en banc) (§455(a) standard warrants consideration of course or pattern of rulings and judge's course of conduct) ("*Moran*"); **(3)** *United States v. Pfizer Inc.*, 456 F.2d 532, 542-44 (8th Cir.), *cert. denied,* 406 U.S. 976 (1927) ("*Pfizer*") (impartiality of judge might reasonably be doubted when judge is finder of fact and before trial states actual settlement amount. The panel's decision conflicts with the decisions of the Supreme Court in **(1)** *Sao Paulo State of Federative Republic of Brazil v. American Tobacco Co. Inc.*, 535 U.S. 229, 232-33 (2002) (§ 455(a) ground for recusal implicates knowledge by a reasonable man of "all the circumstances") ("*Sao Paulo*"); and **(2)** *In re Murchison*, 349 U.S. 133, 136 (1955) (a fair trial in a fair tribunal is a basic requirement of due process) ("*Murchison*").

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[1] Any citation to §455 refers to 28 U.S.C. §455.

FRAP 35(b)(1)(B) STATEMENT: This case presents the following questions of exceptional importance: **(1)** Whether the panel's decision is inconsistent with *In re Kensington*, 368 F.3d 289, 312 (3d Cir. 2004) (timeliness is but one of the factors which engages a court's discretion in determining whether a judge should be relieved from its assignment) ("*Kensington*"); **(2)** Whether the panel's decision is inconsistent with *In re United States of America,* 441 F.3d 44, 48-49, 65 (1st Cir. 2006) ("*In re U.S.A.*") (motion for recusal under §455(a) was timely when filed promptly after last of accumulation of actions by district court over protracted period of time); **(3)** Whether this Court's timeliness doctrine may be invoked to defeat a §455(a) recusal which is predicated on the *Moran* rule, 296 F.3d at 649, that consideration must be given to "a judge's . . . course or pattern of rulings . . . and the judge's course of conduct"; and if so, when does the clock start to run on the course or pattern of rulings and conduct; **(4)** Whether in determining whether §455(a) recusal is warranted because of a judge's course or pattern of rulings and the judge's course of conduct, *Moran*, 296 F.3d at 649, this Court's timeliness doctrine requires the moving party to timely file a motion for recusal after each known separate act which with other separate acts make up the pattern and course of rulings; **(5)** Whether when determining if §455(a) recusal is warranted because the judge's impartiality might reasonably be questioned by the average person on the street who knows all the relevant circumstances, *Moran*, 296 F.3d at 648; *Sao Paulo,*

535 U.S. at 232-233, the circumstances to be considered are subject to any limitation as to time; **(6)** Whether the Court's timeliness doctrine is eviscerated by §455(e); **(7)** Whether the panel's decision conflicts with *Apple v. Jewish Hosp. and Medical Center*, 829 F.2d 326, 333-34 (2d Cir. 1987) (actual time elapsed between events giving rise to charge of bias is not necessarily dispositive; movant may be able to demonstrate good cause for delay, and the analysis of a §455(a) claim must be guided by an independent examination of the facts and circumstances of the particular claim) ("*Apple*"); or with *Liljeberg v. Health Services Acquisition Corp.*[,] 486 U.S. 847, 865 (1988) (it is critically important under §455(a) to identify facts that might reasonably cause objective observer to question impartiality) ("*Liljeberg*") or conflicts with *Potashnick v. Port City Construction Co.*, 609 F.2d 1001, 1111-12 (5th Cir. 1980) (overriding goal by Congress in §455(a) to foster appearance of impartiality also pervades Code of Judicial Conduct and ABA Code of Professional Responsibility); **(8)** Whether the panel's decision is inconsistent with *In re U.S.A.*, 441 F.3d at 56 (under §455(a) standard any reasonable doubts about partiality of judge to be resolved in favor of recusal) or with *Union Planters Bank v. L & J Development Co., Inc.*, 115 F.3d 378, 383 (6th Cir. 1997) (where question close, judge must recuse himself); **(9)** Whether this Court's timeliness doctrine in *Fletcher v. Conoco Pipe Line Co.*, 323 F.3d 661, 664 (8th Cir. 2003) ("*Fletcher*") may be invoked to defeat motions for recusal that are not interposed for tactical or strategic reasons;

(10) Whether the panel's decision implicitly approving the lower court's denial of discovery and a full evidentiary hearing on recusal issues is in conflict with the seminal decision, *Cheeves v. Southern Clays Inc.*, 797 F. Supp. 1570, 1580 (M.D. Ga. 1992) ("*Cheeves*"), *aff'd, without op.*, 39 F.3d 326 (11th Cir. 1994), *cert. denied,* 515 U.S. 1102 (1995) and/or with *Kensington,* 368 F.3d at 323; **(11)** Whether the panel's decision, implicitly approving the interview that Judge Hoyt gave a reporter where Judge Hoyt denigrated TSF, its principals, and its attorney, and where Judge Hoyt told the reporter but never disclosed to TSF's counsel that one of TSF's principal's had "hit on" Judge Hoyt's clerk, is in conflict with the Code of Conduct for United States Judges or with *United States v. Microsoft Corporation,* 253 F.3d, 34, 107-117 (D.C. Cir.), *cert. denied*, 534 U.S. 952 (2001) (interviews of trial judge with news reporters created impression he was not acting impartially as §455(a) requires) ("*Microsoft*") or is in conflict with both; **(12)** Whether the panel's decision, implicitly approving of Judge Hoyt's solicitation of other parties' views in TSE's bankruptcy on the issue of whether Judge Hoyt should recuse himself, and also implicitly approving of Judge Hoyt's incorporating one of TSF's adversary's language at length in Judge Hoyt's opinion declining to recuse himself, is in conflict with Resolution G of the Judicial Conference of the United States, with this Court's decision in *Southwestern Bell Telephone Co v. FCC,* 153 F.3d 520, 521 (8th Cir. 1998) ("*Southwestern*"), or both; or **(13)** Whether Judge Hoyt's implicit decision not to disclose to

counsel for TSF that a principal of TSF had "hit on" the Judge's clerk was unethical, was an abuse of discretion, or both, *U.S. v. Fazio,* 487 F.3d 646, 652-53 (8th Cir. 2007), *cert. denied,* 128 S. Ct. 523 (2007) (standard of review for judge's failure to disclose wife's relationship to government witness is abuse of discretion); and **(14)** Whether unethical conduct by the trial judge requires recusal under either §455(a) or (b).

BACKGROUND

Tri-State Ethanol Co., LLC ("TSE") was formed to build, own, and operate an Ethanol Plant (the "Plant"). On 5/23/03, TSE filed a Chapter 11 case in South Dakota, which was converted to Chapter 7 in July 2004.

Before conversion to Chapter 7, a group of TSE investors had formed TSF to provide funding ($2.5 million) for the Chapter 11 case. Those investors transferred their equity in TSE in exchange for equity in TSF.

On 12/12/03, Judge Hoyt denied TSE's motion for multifaceted relief, refusing to authorize TSE to contract with ICM to retrofit the Plant, to obtain super priority financing from TSF and First Dakota National Bank for such retrofitting, and to grant priming first liens securing that financing.

After such denial and while TSE was still in Chapter 11, ICM undertook to retrofit the Plan[t]

without court approval, believing, on advice of former counsel, that Jude Hoyt's denial of such motion did not prevent TSE and ICM from retrofitting the Plant if there was no contract, no super priority financing, and no first priming liens. The understanding between TSE and ICM, fully disclosed in TSE's approved disclosure statement, was that ICM would not be paid by TSE absent successful retrofitting.

The retrofitting, completed by ICM after conversion to Chapter 7 by agreement between the Trustee and ICM, eventually enabled secured creditors, who would not have been paid in full, to be paid in full, and unsecured creditors, who probably would not have been paid at all, to be paid, probably in full.

Also, after Judge Hoyt had denied TSE's motion for multifaceted relief, on advice of former Counsel, TSF lent TSE $1,983,654.42 to facilitate retrofitting of the Plant, without Judge Hoyt's approval. Of the $1,983,654.42, $763,654.43 was to pay day-to-day expenses and keep the Plant open – necessary for retrofitting to proceed. The balance of $1,190,000 was to pay for equipment necessary for retrofitting the Plant. The $793,654.42 was allowed and paid as a Chapter 11 administrative expense; the $1,190,000 was allowed – but only as a general unsecured claim, subordinated to most other allowed general unsecured claims.

It evolved between July 2004 and May 2006, from certain rulings and conduct, that, in Judge Hoyt's view, TSE, ICM and TSF, in retrofitting

without court approval, violated his December 2003 Order denying TSE's motion for multifaceted relief and should be penalized. No determination that such was the case has ever been made.

ARGUMENT: On 6/29/06, TSF filed a motion under §455(a) and (b) and *Pfizer* for recusal of Judge Hoyt from hearing future disputes involving TSF ("Recusal Motion"). The Recusal Motion was based on the pattern of ongoing rulings and conduct of Judge Hoyt, starting 7/28/04 and fully unfolding in a 5/4/06 hearing.[2] Discovery, a hearing, and an opportunity to

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[2] Such pattern included: conversion of TSE's case to Chapter 7; unnecessary and undeserved comments at time of conversion and thereafter that TSF deliberately violated his rulings based on his "don't ask – seek forgiveness" construct, abused the bankruptcy process and nefariously schemed to increase its equity in TSE; animus toward TSF, its principals, and its attorney; unfair treatment compared to others bidding at the sale of the Plant; unreasonable rulings in adversary proceedings in which TSF was not granted adequate time to prepare; writing "status letters" which were road maps to the Trustee in his litigation against TSF and ICM which focused on lack of prior authorization; insisting that claims of TSE and ICM for costs of retrofitting be demoted from priority status; blaming TSF for breaching settlement agreements with the general contractor that built the Plant, while refusing to look at TSF's documentation showing blame was misplaced; disqualifying involvement in settlement; and upon retirement going on recall status for the purpose of seeing that TSF did not have its $1,190,000 claim allowed with priority or without subordination. Contrary to the panel's opinion, TSF has never claimed that Judge Hoyt's 12/12/03 ruling was a basis on which TSF sought recusal. Reference to that ruling was made only because it is a background fact necessary to explain Judge Hoyt's pattern of conduct.

develop a full record were denied. This recusal was denied on 9/11/06.

A: ***Wrong Issues and Legal Analysis.*** The panel mistakenly framed the issues raised by TSF's Recusal Motion and consequently applied the wrong legal analysis. The major issues raised by TSF's Recusal Motion not considered by the panel are whether accumulation of unfavorable rulings and unfavorable conduct between 7/28/04 and 5/4/06 establish a pattern that require recusal and, if this Court's timeliness doctrine has applicability, whether TSF's Recusal Motion was promptly filed after the pattern existed.

Judge Hoyt's pre-5/4/06 unfavorable rulings and conduct were not sufficient individually for TSF to file its Recusal Motion. The dots were not connected until a 5/4/06 hearing and when the supporting affidavit of Grace (Mimi) Larsen was obtained after 6/12/06. By his 5/4/06 comments and the interview discussed in the affidavit, Judge Hoyt revealed that his earlier rulings and comments could not reasonably be understood in any way except in terms of appearance of bias and actual bias. The 5/4/06 hearing was when Judge Hoyt first disclosed in substance that although retiring he intended to go on recall status to ensure that TSF's claim for $1,190,000 would not have priority and would be subordinate to other general unsecured claims. *Cf. Liteky v. United States*, 540 U.S. 540, 558 (1994) ("If . . . a judge presiding over a retrial should state, based upon facts and opinions formed during the original cause, an

intent to ensure that one side or the other shall prevail, there can be little doubt that he . . . must recuse") (dissent) ("*Liteky*"). This disclosure, coupled with others, demonstrated that Judge Hoyt intended to impose his personal views of justice on TSF instead of following the Bankruptcy Code regarding allowability of claims and priority status of administration claims.[3] *See Matter of Chicago, Milwaukee, St. Paul & Pacific R. Co.*, 791 F.2d 524, 528 (7th Cir. 1986) (fact that a bankruptcy proceeding is equitable does not give judge free floating discretion to redistribute rights in accordance with personal views of justice and fairness).

Contrary to the panel's decision, TSF's Recusal Motion was timely under the rationale that the pattern of rulings and conduct occur over time and a filing after the accumulated acts of the judge is timely. *In re USA; Moran.* Here, the panel measured timeliness from individual rulings or individual instances of conduct, not from the overall pattern. It was unreasonable for the panel to require that TSF

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[3] *See* 11 U.S.C. § 503(b)(1)(A); *In re CoServ, LLC*, 273 B.R. 487, 497 (Bankr.N.D. Tex. 2002) (claims for actual and necessary costs of preserving estate are entitled to priority and include costs of preserving the going concern value); §503(b)(3)(D); *In re Cellular 101, Inc.*, 377 F.3d 1092, 1097 (9th Cir. 2004) (claims for substantial contributions in a Chapter 11 case entitled to priority whether plan confirmed or not). *See also In re Bellanca Aircraft Corp.*, 850 F.2d 1275, 1284-85 (8th Cir. 1988) (court approval under §503(b) not required for allowance of priority claims).

have filed its Recusal Motion before the 5/4/06 hearing and the 6/12/06 Larsen affidavit, because that was before TSF could have made its case for recusal. Moreover, in a 11/18/05 hearing, Judge Hoyt had assured TSE's counsel that he could expect a neutral, objective and fair tribunal. Judge Hoyt's pre-5/4/06 rulings and comments unfavorable to TSF probably did not raise a sufficant [sic] inference of bias. *Moran,* 296 F.3d at 649; *Liteky,* 510 U.S. at 555-56.

This Court and the Supreme Court have made rulings in discrimination cases involving timeliness of claims, which by analogy deserve consideration. *See, e.g., Mems v. City of St. Paul Dept. of Fire and Safety Services*, 327 F.3d 771 (8th Cir. 2002); *Wedow v. City of Kansas City, MO*, 442 F.3d 661 (8th Cir. 2006); *National Railroad Passenger Corp. v. Morgan*, 536 U.S. 101 (2002). These cases deal with the timeliness of claims based on a hostile work environment, which like claims based on a pattern of rulings and conduct, cannot be said to have occurred on a particular day but only over time. Not one of the acts of Judge Hoyt comprising the pattern that later became apparent would have been sufficient for recusal when it occurred. So long as Judge Hoyt's acts were building the pattern and TSF filed its Recusal Motion promptly after the pattern unfolded, the timeliness requirement was met.

B. ***Not Tactical or Strategic:*** There is no evidence that TSF's Recusal Motion was delayed for tactical or strategic reasons. The purpose of this Court's timeliness rule is to avoid the risk that a

party hold its application as an option if the trial court rules against it. *In re Apex Oil Co.*, 981 F.2d 302, 304-05 (8th Cir. 1992). A question of exceptional importance is whether the timeliness doctrine is subject to any limitation that it be invoked only in cases of tactical or strategic advantage.

C. ***Fact Intensive:*** The panel did not discuss in detail the facts underlying the merits of TSF's Recusal Motion. *Moran*, 296 F.3d at 648, confirms that because the test under §455(a) is objective from the perspective of the average person on the street, such person must know "all of the relevant circumstances." *Sao Paulo* confirms that §455(a) recusal requires consideration of "all the circumstances." Do "all relevant circumstances" include rulings and conduct without limitation by this Court's timeliness doctrine; include the absence of tactical or strategic purpose; or include violations of judicial ethics? If the answers are yes, the panel's decision totally eviscerates the "all relevant circumstances" rules of *Moran* and *Sao Paulo* when applied to patterns of rulings and conduct. This raises a question of exceptional importance.

D. ***§455(e):*** §455(e) states in plain, mandatory language: "No . . . judge shall accept from the parties a waiver" of actual bias as a ground for recusal. Section 455(e) also permits waiver of appearance of bias as a ground for recusal only after the judge's full disclosure on the record. These limitations are unfairly evaded if merely characterizing conduct as a forfeiture rather than a waiver defeats recusal. This

Court's decisions in cases such as *Fletcher* do not distinguish clearly when conduct can be characterized as a forfeiture rather than a waiver. *Cf. In re USA.* The question whether a litigant *ever loses the right* to recuse an actually biased or prejudiced judge and ever loses the right to recuse a judge appearing to be partial but not making a full disclosure are questions of exceptional importance.

E. ***Fact Intensive:*** *Liljeberg* holds that under §455(a) it is critically important to identify facts that might reasonably cause an objective observer to question impartiality. *Apple* holds that the question of timeliness does not depend merely upon the time elapsed and the movant can demonstrate good cause for the timing. *Potashnick*, 609 F.2d at 1111-12 (5th Cir.), points out that the legislative history of §455(a) includes an expression by Congress that "(t)he issue of disqualification is a sensitive question of assessing all of the facts and circumstances in order to determine whether the failure to disqualify was an abuse of sound judicial discretion." It also points out that the Congressional view is shared by the judges' and lawyers' professional codes of conduct. A question of exceptional importance is whether the panel was duty bound to do more to assess the merits of TSF's Recusal Motion.

F. ***Settlement:*** Judge Hoyt was too deeply involved in settlement to be fair. *See Pfizer.* Whether a bankruptcy judge that has the duty of approving settlements can be disqualified from deciding a dispute after six times being in on settlement discussions

of the same dispute and stating a flat settlement position for one of the parties is a question of exceptional importance.

G. ***Judicial Ethics:*** Other questions of exceptional importance relate to three potential violations of judicial ethics. First, under *Microsoft* the Recusal Order should be reversed on §455(a) grounds for giving an interview to a reporter about the merits of a pending case in which the judge denigrated TSF, TSF's principals and lawyers, and mentioned that one of TSF's principals had "hit on" his law clerk. Second, Judge Hoyt's decision not to recuse himself on §455(a) grounds for soliciting and relying on opinions of other parties is inconsistent with Resolution G of the Judicial Conference of the United States and the holding in *Southwestern Bell Telephone Co. v. FCC,* 153 F.3d 520, 521 n.1 (8th Cir. 1998). Third, failure to disclose the "hit on" incident to TSF's counsel is a self-evident violation of ethics. Each of the foregoing violations present questions of exceptional importance.

H. ***Full Record:*** The panel implicitly upheld the denial to TSF of any right of discovery, any hearing, and any opportunity to make a full record on the recusal. That decision conflicts with *Skywalk,* and is inconsistent with *Cheeves* and *Kensington.* Under the totality of circumstances of this case, a question of exceptional importance is whether TSF was entitled to discovery, a hearing, and a full record.

I. *Fair Trial:* *Murchison* underscores TSF's constitutional right to a fair trial before a fair tribunal. The panel's conflict with *Murchison* requires TSF to litigate disputes involving millions of dollars before a judge that appears to be actually biased against TSE.

PRAYER

Wherefore, Appellant Tri-State Financial, LLC, respectfully prays for a rehearing en banc and any other relief to which it may be entitled.

Respectfully submitted this 27th day of May, 2008

TRI-STATE FINANCIAL, LLC,
Appellant,

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OPPOSITION BRIEF

Supreme Court, U.S.
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In The
Supreme Court of the United States

TRI-STATE FINANCIAL, LLC,

Petitioner,

v.

JOHN S. LOVALD, TRUSTEE OF THE CHAPTER 7 ESTATE OF TRI-STATE ETHANOL CO., LLC, *et al.*,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

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QUESTIONS PRESENTED

Respondent John S. Lovald, Trustee of the Chapter 7 Estate of Tri-State Ethanol Co., LLC, restates the questions presented as follows:

1. Whether the court of appeals erred in holding that Petitioner's motion to recuse a bankruptcy judge, which was filed thirty months after the first and seven months after the last conduct of which Petitioner complains, and which the bankruptcy court found was made in bad faith, was untimely under 28 U.S.C. § 455?

2. Whether the decision by the court of appeals conflicts with principles established by this Court or any other court of appeals?

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28 U.S.C. § 455 ..... *passim*

STATEMENT OF THE CASE

A. Introduction

The Petitioner, Tri-State Financial, LLC ("Tri-State"), seeks review of the Eighth Circuit's decision that it did not timely file a motion to recuse the bankruptcy judge under 28 U.S.C. § 455. Having lost a number of motions, Tri-State followed the same deliberate course of action that it pursued consistently in bankruptcy court: it chose to attack the integrity of its opposing parties, their counsel, and, ultimately, the integrity of the court. Thirty months after the first alleged conduct of which it complained, Tri-State moved that the bankruptcy judge recuse himself because his impartiality might reasonably be questioned, and for personal bias or prejudice under § 455(a) and (b)(1). In an extensive, 117-page decision, the bankruptcy judge denied the motion. (App. 66-194.)[1] The court considered and rejected each of six bases for recusal on the merits, and also concluded that the motion was untimely. On appeal from the decision denying recusal, the district court concluded that the "recusal motion was not made in good faith but for the improper purpose of further delay and harassment of the trustee, other attorneys, creditors, and the judges." (App. 34.) The district court also concluded that the motion was untimely and should be affirmed on "the basis of untimeliness alone." (*Id.*)

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[1] All citations to the Appendix are to the Petitioner's Appendix.

The Eighth Circuit did not address the merits of the recusal motion, but concluded that it was untimely; the judgment was affirmed on that basis alone. (App. 6-7.)

The Eighth Circuit's decision does not warrant review by the Supreme Court of the United States. The Eighth Circuit's adherence to the timeliness doctrine under § 455, requiring that a party "raise a claim at the earliest possible moment after obtaining knowledge of facts demonstrating the basis for such a claim," *Fletcher v. Conoco Pipeline Co.*, 323 F.3d 661, 664 (8th Cir. 2003), is not novel; neither the timeliness doctrine nor the court's application of the doctrine to Tri-State's motion conflicts with principles established by this Court or by any other court of appeals; and the decision implicates no overriding point of federal law on which further guidance from this Court is needed.

B. The Relevant Facts

Tri-State Ethanol, LLC ("TSE") owned an ethanol plant in Rosholt, South Dakota, that filed a voluntary Chapter 11 bankruptcy petition in May, 2003. (App. 66-67.) Petitioner Tri-State Financial, LLC ("Tri-State"), is a subsequently-formed LLC that sought to invest money in TSE to rebuild its ethanol plant. (App. 73.) During the pendency of the Chapter 11 case, TSE filed a motion, with Tri-State's support, seeking approval to procure post-petition financing secured by a post-petition lien on all of TSE's

pre-petition assets, and to contract for the re-engineering of TSE's ethanol plant. (App. 74-82.) After an evidentiary hearing, the bankruptcy court denied the motion. (App. 86-89.) Neither TSE nor Tri-State appealed from the denial. (App. 89.) Instead, Tri-State ignored the order, and advanced funds to TSE. Re-engineering work proceeded at the plant without court approval. (App. 94-95, 102-104.)

TSE filed a Chapter 11 plan. (App. 89.) The U.S. Trustee brought a competing motion to dismiss TSE's case, or alternatively, to convert it to Chapter 7. (App. 93.) After an evidentiary hearing, the bankruptcy court converted the case in July, 2004. No party appealed. (App. 106-107.)

Eventually, Respondent Chapter 7 Trustee John S. Lovald ("Lovald"), sold the plant on behalf of TSE's Chapter 7 bankruptcy estate to Tri-State in early February of 2005. (App. 117-123.) No party, including Tri-State, appealed from any aspect of the bankruptcy court's or Lovald's handling of the sale.

Tri-State filed an application for administrative expense on January 24, 2005. Tri-State claimed priority for just less than $2 million of its claims against TSE's Chapter 7 estate. (App. 124.) The claim related primarily to the funds Tri-State advanced to TSE without the bankruptcy court's permission. Lovald objected to Tri-State's proof of claim, noting the lack of court approval for the funds advanced. (App. 159-160.) Ultimately, Tri-State and Lovald settled this matter. Despite Tri-State's violation of the

bankruptcy court's orders, its claim was allowed, with $793,000 allowed as an administrative expense, and the balance, $1,190,000, allowed as a general unsecured claim that was subordinated to the claims of other unsecured creditors. (App. 126.) Lovald's motion approving the settlement was granted without objection. (App. 142.) Tri-State did not appeal.

The ink on the order was barely dry when Tri-State filed a motion for recusal on June 29, 2006, seeking recusal of the bankruptcy judge, the Honorable Irvin Hoyt. (App. 146-147.) In its motion, Tri-State raised issues under 28 U.S.C. §§ 455(a) and (b), the doctrine enunciated in *United States v. Pfizer, Inc.*, 560 F.2d 319 (8th Cir. 1977), and the Due Process Clause of the United States Constitution. The motion enumerated six "bases for bias." (*Id.*) Tri-State supported its motion with an affidavit from Grace "Mimi" Larsen, a reporter from the Rosholt area who attended the hearings regarding the sale of TSE's ethanol plant. (App. 160-162.) Lovald timely objected. (App. 147.)

C. The Decisions Below

The bankruptcy court denied Tri-State's recusal motion on September 1, 2006. (App. 65.) The bankruptcy court filed a thorough 117-page decision addressing both timeliness and the merits. (App. 66-194.)

Tri-State filed three notices of appeal to the district court from the recusal order and three other

final, unrelated orders. (App. 15, 20.) Tri-State filed an overlength brief on recusal and the fees of one of the Respondents, attorney Robert Hayes. (App. 35.) On Hayes's motion, the district court struck Tri-State's brief, not only because it was overlength, but also because it contained "scandalous" materials. (*Id.*) Tri-State's brief assailed the integrity of the bankruptcy court, and contained personal attacks on the bankruptcy judge and other members of the bar, including referring to the bankruptcy court as a "kangaroo court" and suggesting that Lovald and his attorney were "under the thumb" of the bankruptcy court. (App. 21-22.)

The district court permitted Tri-State to file another brief, after which, on May 17, 2007, the district court entered an order affirming the order denying recusal. (App. 13-63.) Tri-State then appealed all of the issues resolved by the district court to the Eighth Circuit, which affirmed. (App. 1-12.) The Eighth Circuit cited existing precedent that recusal motions "'will not be considered unless timely made,'" and that a party must raise a claim "'at the earliest possible moment after obtaining knowledge of facts demonstrating the basis for such a claim.'" (App. 5-6 (quoting *Fletcher v. Conoco Pipeline Co.*, 323 F.3d 661, 664 (8th Cir. 2003)).) The Eighth Circuit then concluded that the motion was untimely, and was properly denied on that basis alone. (*Id.* at 6.)

D. Misstatements of Fact in the Petition

Pursuant to Supreme Court Rule 15.2, Lovald notes the following misstatements of fact in the Petition:

1. On page 4, paragraph (a), Tri-State questions whether it was "an abuse of discretion or a denial of [petitioner's] due process rights for the bankruptcy judge to deny TSF discovery, a hearing, and an opportunity to make a full record." This statement implies that the judge Tri-State sought to recuse, the Honorable Irvin Hoyt, denied discovery. To the contrary, Tri-State's motion to depose Lovald was referred by the bankruptcy court to a different bankruptcy judge, the Honorable Robert Kressel, sitting by designation of the Eighth Circuit Court of Appeals. Judge Kressel denied Tri-State's motion for discovery. (App. 24.)

2. On page 12, note 6, Tri-State indicates that the reporter signed her supporting affidavit on June 12, 2006, thereby suggesting that the events detailed in the affidavit were contemporaneous. To the contrary, the alleged events detailed in the affidavit occurred nearly two years earlier, in October, 2004. (App. 6.)

3. On page 14, Tri-State states that "the bankruptcy judge denied [Petitioner's] timely requests for discovery." As indicated, a different judge, Judge Kressel, made the ruling in question. (App. 24.)

4. On page 14, Tri-State also states that the bankruptcy judge conducted a "straw poll" of the attorneys representing other litigants in TSE's Chapter 7 case, "requesting their views concerning the recusal motion." This assertion is not supported in the record. The docket reveals that the court, in response to Tri-State's motion, set a deadline for "joinders and responses," just as for other motions in the case. (App. 34.)

REASONS FOR DENYING THE WRIT

1. The Eighth Circuit's decision is consistent with this Court's rule that courts have inherent power to prevent bad-faith litigation conduct.

Courts have the inherent power to prevent and sanction bad-faith conduct. *See, e.g., Chambers v. NASCO, Inc.*, 501 U.S. 32, 46, *reh'g denied*, 501 U.S. 1269 (1991). The Eighth Circuit's timeliness rule prevents bad faith. As noted by the Eighth Circuit in finding Tri-State's recusal motion untimely, "[a] party is required to bring its recusal motion promptly to avoid the risk that the party might hold its application as an option in the event the trial court rules against it." *Tri-State Financial, LLC v. Lovald*, 525 F.3d 649, 653 (8th Cir. 2008) (citing *In re Apex Oil Co.*, 981 F.2d 302, 304-05 (8th Cir. 1992)). Because recusal motions are often a litigation tactic, they must be brought as soon as

the party bringing the motion possesses the facts upon which the motion is based. *See, e.g., In re Cargill, Inc.*, 66 F.3d 1256, 1262-63 (1st Cir. 1995).

The bankruptcy and district courts found that Tri-State acted in bad faith. Unable to prevail on the merits of its claims in TSE's bankruptcy case, and apparently unwilling to appeal from the adverse rulings, Tri-State resorted to personal attacks on two bankruptcy judges, Lovald, and Lovald's counsel. In Tri-State's original motion to recuse, Tri-State accused the bankruptcy judge of bias and prejudice over more than two years, from May 2003 through December 2005. (App. 6.) Despite not appealing from any of the rulings, Tri-State then sought discovery to support its motion, which request was transferred to the Honorable Robert J. Kressel, United States Bankruptcy Judge for the District of Minnesota. (App. 24-25.) Judge Kressel denied the motion, noting that Tri-State had failed to cite any supporting authority, and failed to indicate what information it sought through discovery. Tri-State then filed a motion for reconsideration suggesting that Judge Kressel acted without reading Tri-State's submissions (App. 21, 24-25), and claiming that Judge Kressel lacked the authority to decide the motion. (App. 24.)

Tri-State's conduct got worse on appeal to the district court. Tri-State referred to the procedure as "bordering on blackmail" and a "kangaroo court." (App. 21-22.) Tri-State further claimed, without any supporting evidence, that various decisions were nothing more than "road maps" the bankruptcy court

issued for Lovald's benefit. (*Id.*) Tri-State even argued that a judge from another state should take over because no judge from South Dakota could properly handle the case. (App. 21.)

Tri-State did not limit its assault to the bankruptcy court. It suggested that Lovald and his counsel, Respondent Robert Hayes, were "under the thumb" of the bankruptcy judge. (App. 22.) Tri-State also belatedly attacked special counsel's application for fees, claiming that Respondent Hayes had a conflict of interest. (App. 10-12.)

Tri-State's motion for recusal was a litigation tactic. The decisions of the bankruptcy court, the district court, and the Eighth Circuit refusing to countenance Tri-State's conduct are consistent with well-established law.

2. The Eighth Circuit's decision is not in conflict with the decisions of this Court or any other circuit.

Tri-State has not claimed that its motion was timely. Instead, Tri-State tries to manufacture a circuit split. While the circuits have produced various formulations of the timeliness rule, Lovald is unaware of any current recusal rule from any court of appeals that has rejected timeliness as Tri-State argues. Instead, following this Court's decision in *Liljeberg v. Health Services Acquisition Corp.*, 486

U.S. 847 (1988),[2] every circuit that has considered the issue appears to have imposed some formulation of the rule in order to prevent bad-faith filings like Tri-State's. *See, e.g., In re United States*, 441 F.3d 44, 65 (1st Cir. 2006) ("[C]ourts will reject what appear to be strategic motions to recuse a judge whose rulings have gone against the party. That is why, in general, a party must raise the recusal issue 'at the earliest moment after [acquiring] knowledge of the [relevant] facts.'"); *United States v. Amico*, 486 F.3d 764, 773 (2d Cir. 2007) ("To ensure that a party does not 'hedg[e] its bets against the eventual outcome' of a proceeding, a party must move for recusal 'at the earliest possible moment after obtaining knowledge of facts demonstrating the basis for such a claim.'") (citations omitted); *United States v. Owens*, 902 F.2d 1154, 1156 (4th Cir. 1990) (stating that timeliness applies to motions under both § 144 and § 455); *Travelers Ins. Co. v. Liljeberg Enterprises, Inc.*, 38 F.3d 1404, 1410 (5th Cir. 1994) ("it is well-settled that – for obvious reasons – one seeking disqualification must do so at the earliest moment after knowledge of the facts demonstrating the basis for such disqualification"); *Schurtz Communications, Inc. v. FCC*, 982 F.2d 1057, 1060 (7th Cir. 1992) (stating that motion was too late, and questioning whether single weak case rejecting timeliness was still good authority); *Edgar v. K.L.*, 93

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[2] "[A] delay of 10 months after the affirmance by the Court of Appeals would normally foreclose relief based on a violation of 455(a). . . ." *Liljeberg*, 486 U.S. at 869.

F.3d 256, 258 (7th Cir. 1996) ("parties who know of a problem under § 455 but permit the trial to occur may not seek relief later"); *Preston v. United States*, 923 F.2d 731, 733 (9th Cir. 1991) ("[w]e require recusal motions to be lodged in a timely fashion because the absence of such a requirement would result in increased instances of wasted judicial time and resources . . . and a heightened risk that litigants would use recusal motions for strategic purposes"); *United States v. Pearson*, 203 F.3d 1243, 1276 (10th Cir. 2000) ("A promptly filed motion conserves judicial resources and alleviates the concern that it is motivated by adverse rulings or an attempt to manipulate the judicial process."), *cert. denied*, 530 U.S. 1268 (2000); *United States v. Slay*, 714 F.2d 1093, 1094 (11th Cir. 1983); *United States v. Barrett*, 111 F.3d 947, 951-52 (D.C. Cir. 1997) (collecting cases), *cert. denied*, 522 U.S. 867 (1997).

a. The Sixth, Seventh and Ninth Circuits have not rejected a timeliness rule.

Contrary to Tri-State's argument, the Sixth, Seventh, and Ninth Circuits do not reject the timeliness doctrine. (Petition at 20-25.) The Sixth Circuit has never expressly addressed the timeliness issue, as Tri-State admits. (Petition at 23.) Tri-State's argument that the Sixth Circuit has found § 455 to be "self-executing," moreover, does not foreclose a timeliness requirement. The Sixth Circuit has never held this to be the case, and other courts have rejected the argument. *See, e.g., E & J Gallo Winery v. Gallo*

Cattle Co., 967 F.2d 1280, 1295 (9th Cir. 1992) ("[§ 455] is self-enforcing on the part of the judge. . . . However, it does not necessarily follow that a party having information that raises a possible ground for disqualification can wait until after an unfavorable judgment before bringing the information to the court's attention. It is well established in this circuit that a recusal motion must be made in timely fashion.")

Cases from the Seventh and Ninth Circuits decided after those Tri-State cites demonstrate that timeliness is decisive in those circuits as well. *See, e.g., Schurtz Communications, Inc.*, 982 F.2d at 1060 (stating that motion was "too late"); *Edgar*, 93 F.3d at 258 ("parties who know of a problem under § 455 but permit the trial to occur may not seek relief later"); *Preston v. United States*, 923 F.2d 731, 733 (9th Cir. 1991) ("We require recusal motions to be lodged in a timely fashion. . . ."); *Skokomish Indian Tribe v. United States*, 410 F.3d 506, 519 (9th Cir. 2005) (motion for recusal must be timely), *cert. denied*, 546 U.S. 1090 (2006).

b. Decisions that timeliness is a factor do not conflict with the Eighth Circuit's decision.

The Eighth Circuit's decision does not conflict with decisions from the Third Circuit and the Federal Circuit. (Petition at 25.) The Third Circuit did not reverse the denial of a recusal motion in *In re*

Kensington Int'l, Ltd. because the court below had applied the timeliness rule. Rather, it reversed and remanded because the court had applied the rule improperly by unfairly imputing constructive knowledge of the bases for disqualification to the party seeking recusal, when actual knowledge did not exist. 368 F.3d 289, 312-313 (3d Cir. 2004).

The Federal Circuit does not have a timeliness rule of its own. Recusal issues are unrelated to substantive patent law. In matters unrelated to patent law, such as recusal, the Federal Circuit must follow the guidance of the regional circuit in which the district court ruling on the motion sat, not a rule of its own. *Polaroid Corp. v. Eastman Kodak Co.*, 867 F.2d 1415, 1419 n. 11 (Fed. Cir. 1989) (citing First Circuit cases applying timeliness rule). Consequently, even the *Polaroid* court, following the timeliness rule from the First Circuit, found the passage of time to be decisive. *Id.* at 1419 ("the circumstances of the present case form a far more compelling basis for imposing such a requirement than any appearing in the cited cases").

c. The First Circuit's reference to an "accumulation of events" does not create a conflict.

The First Circuit's reference to an "accumulation of events" in *In re United States*, 441 F.3d 44, 65-68 (1st Cir.), *cert. denied*, 127 S.Ct. 288 (2006), is not contrary to the Eighth Circuit's decision in this case.

(Petition at 26-27.) Notably, the First Circuit did not establish a timeliness standard. *Id.* at 65 ("[t]his court has not stated a standard of review for a holding by a district court that a recusal motion is untimely"). Rather, the First Circuit held that "[u]nder any standard, we reject the preliminary argument that the recusal motion came too late." *Id.* The court argued, however, that "in general, a party must raise the recusal issue 'at the earliest moment after acquiring knowledge of the relevant facts.'" *Id.* (quoting *In re Abijoe Realty Corp.*, 943 F.2d 121, 126 (1st Cir. 1991)).

There is no conflict on the facts of this case. The Eighth Circuit noted, and Tri-State's counsel conceded at oral argument, that the events forming the basis for Tri-State's recusal motion first occurred nearly three years before the recusal motion, and last occurred nearly seven months before. Even under the "accumulation" standard, this was a disqualifying delay, particularly given Tri-State's delay in filing its motion until *after* the bankruptcy court approved Tri-State's disputed claim against TSE's estate.

d. The Fifth, Ninth, and Eleventh Circuits have not rejected a timeliness rule.

Tri-State's arguments about a *per se timeliness* rule rest upon a fundamental misunderstanding of what its own authority says. (Petition at 27-28.) While in *Andrade v. Chojnacki,* the Fifth Circuit declined to establish a bright line establishing when a

recusal motion is too late, it went on to state that "generally, such motions must be filed 'at the earliest moment' after a movant receives knowledge of the facts suggesting disqualification." 338 F.3d 448, 459 n. 5 (5th Cir. 2003) (quoting *Travelers Ins. Co.*, 38 F.3d at 1410). Similarly, in *E & J Gallo Winery v. Gallo Cattle Co.*, the Ninth Circuit stated that "there is no *per se* rule that recusal motions must be made at a fixed point in order to be timely," but in the same sentence also held that "such motions 'should be filed with reasonable promptness after the ground for such a motion is ascertained,'" and that "[i]t is well established in this circuit that a recusal motion must be made in timely fashion." 967 F.2d at 1295. Finally, in *Summers v. Singletary*, the Eleventh Circuit expressly declined to adopt a *per se* rule regarding timeliness, but in the next sentence stated "[w]e hold that a motion to disqualify filed under § 455(b) must be filed within a reasonable time after the grounds for the motion are ascertained." 119 F.3d 917, 921 (11th Cir. 1997), *cert. denied*, 525 U.S. 1165 (1999).

The *per se* rule that these courts rejected was a rule based on a certain time period, not a rule that an untimely motion could not be denied for that reason alone. These courts, instead of imposing a bright-line rule, have held that the motion must be filed within a "reasonable time." Given Tri-State's decision to wait until thirty months after the first alleged evidence and seven months after the last alleged evidence of grounds for recusal had arisen, the Eighth Circuit's decision that Tri-State did not act within a reasonable

time does not conflict with the law in the Fifth, Ninth, and Eleventh Circuits.

3. There is no confusion or uncertainty among the circuits regarding waiver.

Tri-State argues that "there is inconsistency among the circuits regarding how, if at all, theories of waiver and forfeiture intersect with timeliness considerations in § 455 motions." (Petition at 30.) By suggesting that waiver and forfeiture do not apply to § 455 issues, Tri-State conflates two separate issues. Waiver and forfeiture are not issues here because, unlike in the cases Tri-State cites, recusal was not raised for the first time on direct appeal.

In *Fletcher v. Conoco*, 323 F.3d 661 (8th Cir. 2003), the Eighth Circuit discussed waiver and forfeiture because recusal was raised for the first time on direct appeal. *Id.* at 663. Indeed, that is the factual scenario presented in nearly all of the cases Tri-State cites. *See United States v. Mathison*, 157 F.3d 541, 545-46 (8th Cir. 1998) ("[defendant] chose not to raise the matter of recusal before the trial court, although he plainly thought that he might have a basis for asking the judge to recuse.") (citations omitted); *see also United States v. Bayless*, 201 F.3d 116, 127 (2d Cir. 2000) (analyzing whether failure to make a recusal motion below was fatal to claim on appeal); *cf. United States v. Murphy*, 768 F.2d 1518, 1540 (7th Cir. 1985) (analyzing whether recusal issue raised for first time post-trial, and post-sentencing was waived).

The parties in all of these cases violated the well-established rule from *United States v. Olano*, 507 U.S. 725 (1993), that issues should, if possible, be presented to the trial court to avoid wasting the time and expense of trial. *Id.* at 731 ("'No procedural principle is more familiar to this Court than that a constitutional right', or a right of any other sort, 'may be forfeited in criminal as well as civil cases by the failure to make timely assertion of the right before a tribunal having jurisdiction to determine it'."). Failure to raise an issue below affects the standard of review on appeal. *See Fletcher*, 323 F.3d at 664 (citing *Olano* and holding that when a party waits until appeal to raise a recusal claim for the first time, appellate review is only for plain error); *Mathison*, 157 F.3d at 546 (citing *Olano*); *Bayless*, 201 F.3d at 127-28 (citing *Olano* and holding that issues raised for the first time on appeal, including recusal, are reviewed only for plain error); *Murphy*, 768 F.2d at 1542 ("[a] criminal trial is too serious and too costly to permit a defendant to sit on possible errors, hoping to have a crack at an acquittal (or low sentence) and then still a second trial") (citing *Margoles v. Johns*, 660 F.2d 291 (7th Cir. 1981) (appearance of impropriety, and perhaps even actual impropriety, may not be raised for the first time on collateral attack), *cert. denied*, 455 U.S. 909 (1982)).

This case does not present an issue of waiver or forfeiture, but of untimeliness. One of the cases Tri-State cites, *Bayless,* aptly describes the distinction. "Waiver is a renunciation – whether expressly

through words or implicitly through behavior – of the right to seek recusal. Untimeliness, on the other hand, is merely a failure to seek recusal when it should first have been sought, that is, as soon as the facts on which it is premised are known to the parties." *Bayless*, 201 F.3d at 127. The Eighth Circuit's timeliness rule in the context of the case before the court, has nothing to do with the issue of waiver as articulated in *Mathison, Conoco,* or *Olano.*

4. Tri-State's collateral arguments do not provide compelling reasons to grant the Petition.

Tri-State has raised two collateral issues, neither of which implicates a circuit split, a conflict with a decision of this Court, or an issue of utmost importance requiring this Court's exercise of *certiorari* review.

a. The Eighth Circuit's decision does not subvert the judicial canons.

In an effort to suggest that the Eighth Circuit's decision excuses conduct that violates the judicial canons, Tri-State continues its assault on Judge Hoyt by relying upon the affidavit of Grace "Mimi" Larsen, a Rosholt area reporter. The unsubstantiated and hearsay allegations made in Larsen's affidavit, as noted by the district court, were speculative, conjectural, and conclusory, as opposed to factual or unbiased. The district court noted that the affidavit was

filled with opinions and conclusions rather than facts, likened the bankruptcy court to a "kangaroo court" and the proceedings to "blackmail," and referred to unnamed people who would be unhappy with the court's ruling. (Petitioner's App. 22.) Such rumor and innuendo, even when published – which was not the case here – does not support disqualification:

> "Although public confidence may be as much shaken by publicized inferences of bias that are false as by those that are true, a judge considering whether to disqualify himself must ignore rumors, innuendos, and erroneous information published as fact in the newspapers. . . . To find otherwise would allow an irresponsible, vindictive or self-interested press informant and/or an irresponsible, misinformed or careless reporter to control the choice of judge."

United States v. Cooley, 1 F.3d 985, 994 (10th Cir. 1993) (quoting *United States v. Greenough*, 782 F.2d 1556, 1558 (11th Cir. 1986)).

Tri-State's argument attempts to inject the merits of Tri-State's recusal motion into its Petition. Whether Tri-State's Petition should be granted, however, depends on whether the Eighth Circuit's affirmance on timeliness grounds creates a split among the circuits, contradicts a decision of this Court, or implicates an overriding point of federal law on which further guidance from this Court is needed. Because Tri-State's view of the merits through Larsen's affidavit does not implicate these

concerns, Tri-State's effort is just one more example of Tri-State's litigation conduct.

b. Petitioner had no right to discovery or a hearing.

Tri-State finally attempts to inflate this case into one presenting an important question of due process. By its own admission, however, Tri-State did not have a right to discovery or a formal hearing on its motion for recusal.[3] (Petition 36, n. 18.) Tri-State's own authority confirms the bankruptcy court's broad discretion regarding discovery and a hearing. The issue simply does not require this Court's attention.

Tri-State cites no authority clearly supporting its argument. In *Moran v. Clarke*, 296 F.3d 638 (8th Cir. 2002), the court mentions in passing that an inquiry under 28 U.S.C. § 455 into judicial bias requires knowledge of "all of the relevant facts," but contains no discussion whether a party bringing a recusal motion is entitled to discovery. The same is true of *In re Federal Skywalk Cases*, 680 F.2d 1175 (8th Cir. 1982), which contains no discussion of any party's entitlement to discovery in conjunction with a recusal motion.

No case Tri-State cites that discusses discovery in the context of recusal mandates discovery or a

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[3] The only discovery Tri-State sought was a deposition of, and limited written discovery to, the Trustee.

hearing. The decision in *In re Kensington Int'l, Ltd.*, 353 F.3d 211, 223 (3rd Cir. 2003) (Petition at 37) is distinguishable. In *Kensington*, the Third Circuit held that the district court should have permitted discovery on recusal, but did not hold that discovery is mandatory in all recusal cases. The party *seeking recusal*, moreover, opposed discovery. These facts do not exist here, especially given that Tri-State has failed to articulate a single fact not already in the record it sought to discover. The decision in *Cheeves v. Southern Clays, Inc.*, 797 F. Supp. 1570 (M.D. Ga. 1992) (Petition at 36), actually supports Judge Kressel's denial of discovery. The court in *Cheeves* held that discovery is appropriate only in limited circumstances, and only upon an adequate showing of good cause. *Id.* at 1580.

Thus, Tri-State's own authority recognizes that a party seeking discovery on a recusal motion must demonstrate good cause or a genuine need for discovery. *Id.* at 1580 n. 17. In fact, the court in *Cheeves* held: (1) that compulsory discovery from a trial judge related to that judge's recusal is almost per se impermissible, *id.* at 1583; and (2) that the party moving for recusal had failed to prove the need for discovery. *Id.* at 1584. In this case, the bankruptcy judge sitting by designation on Tri-State's discovery motion similarly found that Tri-State had failed to meet its burden.

A myriad of other authorities supports denial of Tri-State's motion for discovery as well. *See, e.g., Goodwin v. Durkin*, 194 B.R. 214, 226 (B.A.P. 9th Cir.

1996) ("a motion to recuse is not a mere pleading, a first step towards a possible case. Like any public official, a judge is presumed to be qualified to act, and an objector must come with a prima facie case, not just a hope of developing one. . . .") (citing *Ricci v. Key Bancshares of Maine, Inc.*, 111 F.R.D. 369, 373 n. 4 (D. Me. 1986) (holding that district court had not committed error by refusing to permit a party moving for recusal to conduct depositions); *Lyeth v. Chrysler Corp.*, 929 F.2d 891, 899 (2d Cir. 1991) (holding that district court properly denied requests for discovery)); *see also State of Idaho v. Freeman*, 507 F. Supp. 706, 730 (D. Idaho 1981) ("A motion to disqualify under section 455 is not based on the sufficiency of a party's pleadings or allegations, thus an evidentiary hearing or discovery is not required to establish disputed facts.")

A court's discretion to hold, or not hold, a hearing regarding recusal is equally well-established. *See, e.g., United States v. Cherry*, 330 F.3d 658, 666 (4th Cir. 2003) ("contrary to [defendant's] contention, the court was not required to conduct an evidentiary hearing on the recusal issue"); *Travelers Ins. Co. v. Liljeberg Enter., Inc.*, 38 F. 3d at 1408 n. 4; *United States v. Kanahela*, 951 F. Supp. 928, 945 (D. Hawaii 1996) ("the trial judge may elect to hold a hearing on the motion or, if insufficient facts have been alleged to warrant a hearing may simply decline to recuse herself"); *Freeman*, 507 F. Supp. at 729 n. 30; *In re Haney*, 238 B.R. 427, 429 n. 3 (Bankr. E.D. Ark. 1999) ("evidentiary hearings on motions to recuse are not

necessary, nor, in many instances, appropriate"); *In re Lieb*, 112 B.R. 830, 836 (Bankr. W.D. Tex. 1990) ("[a] motion for disqualification does not confer upon Defendants a right to make a record in open court nor does it confer upon them a right to an evidentiary hearing").

Because Tri-State had no right to conduct discovery and no right to a hearing, Tri-State's due process concerns are unfounded.

CONCLUSION

The Court should deny the petition for certiorari.

Respectfully submitted,

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REPLY BRIEF

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No. 08-369

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In The

Supreme Court of the United States

TRI-STATE FINANCIAL, LLC,

Petitioner,

v.

JOHN S. LOVALD, TRUSTEE OF THE CHAPTER 7 ESTATE OF TRI-STATE ETHANOL CO., LLC, *et al.*,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

PETITIONER'S REPLY TO RESPONDENT LOVALD'S BRIEF IN OPPOSITION

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REPLY

RESPONDENT'S UNSUPPORTABLE ALTERATION OF THE QUESTIONS PRESENTED RENDERS THE OPPOSITION UNRESPONSIVE TO THE VITAL ISSUE AT HAND – THE PUBLIC'S FAITH IN THE FEDERAL JUDICIARY

Respondent attempts to distract this Court by supplanting the questions central to the Petition with questions not properly before the Court. The crucial questions are whether the Eighth Circuit may elevate its timeliness doctrine so as to avoid review of a 28 U.S.C. § 455 recusal motion on the merits and whether such doctrine puts in jeopardy the public's faith in the integrity, impartiality and independence of the federal judiciary.

A. Altered Questions. In rewriting Question I, Respondent ignores whether the Eighth Circuit's timeliness doctrine may be elevated to a rule of first resort and controlling importance in deciding § 455 motions without reference to the merits. In rewriting Question II, Respondent omits the risk of undermining the public's confidence in the integrity of the federal judiciary. Respondent's efforts to minimize and demote this crucial issue of national importance to a parochial request for correction of a perceived injustice based on a factual dispute (Opp. 19-20) should not be countenanced.

B. Established *Sao Paulo/Liljeberg* Law. Respondent ignores *Sao Paulo State of Federative*

Republic of Brazil v. American Tobacco Co., 535 U.S. 229 (2002), which requires courts, in ruling on § 455 motions, to consider "all the circumstances"; and also ignores *Liljeberg v. Health Services Acquisition Corp.*, 486 U.S. 847 (1988), instructing that it is "critically important" to identify circumstances giving rise to an objective appearance of partiality. (Petition 18-20.) The decision below conflicts with *Sao Paulo* and *Liljeberg*.

C. Inconsistent Timeliness Analyses. Respondent makes no legitimate argument that the law regarding the effect of timeliness on § 455 is settled and uniform. As detailed in the Petition, the circuits do not agree, and the state of the law within some circuits is uncertain. The cases cited by Respondent do not undercut Petitioner's analysis. Indeed, Respondent has conceded that " . . . the circuits have produced *various formulations* of the timeliness rule. . . . " (Opp. 9) (emphasis added.)

Contrary to Respondent's argument, *In re Kensington Int'l Ltd.*, 368 F.3d 289, 312 (3d Cir. 2004) instructs that "timeliness . . . is but one of the factors. . . . " *Accord Polaroid Corp. v. Eastman Kodak Co.*, 867 F.2d 1415, 1418 (Fed.Cir. 1989). To argue that the decision below does not conflict with those holdings (Opp. 12-13) is folly.

To argue that *In re U.S.*, 441 F.3d 44, 65-68 (1st Cir. 2006) does not conflict with the decision below is likewise untenable. There, the First Circuit recognized, as did the Third Circuit in *Kensington*, that

timeliness is but one factor; and that time must be allowed for disqualifying events to accumulate, with timeliness measured from the last event.

Respondent erroneously contends that the Sixth, Seventh, and Ninth Circuits have not rejected a timeliness rule. (Opp. 11.) The plain language of *SCA Services Inc. v. Morgan,* 557 F.2d 110, 117 (7th Cir. 1977), expressly declares otherwise. (Petition 22.) The finding in *Easley v. University of Michigan Bd. of Regents,* 853 F.2d 1351 (6th Cir. 1988), that § 455 is self-executing and in *In re Manoa Finance Co.,* 781 F.2d 1370 (9th Cir. 1986), that it imposes a self-enforcing obligation upon the judge imply the absence of any timeliness requirement. (Petition 23-24.)

Respondent's reference to *In re Cargill, Inc.*, 66 F.3d 1256 (1st Cir. 1995), suggesting that, to avoid the appearance of tactical manipulation, recusal motions should be brought as soon as a movant possesses sufficient facts (Opp. 7-8) does not alter the observation of the First Circuit in *In re U.S., supra.* Respondent similarly references tactics by citing *U.S. v. Amico*, 486 F.3d 764, 773 (2d Cir. 2007). (Opp. 10.) Respondent ignores *Amico* also instructs that, in evaluating timeliness, courts look to four enumerated factors, thus reinforcing *Apple v. Jewish Hosp. and Medical Center*, 829 F.2d 326 (2d Cir. 1987) (finding elapse of time not dispositive; timeliness must be evaluated through a comprehensive, independent examination of facts and circumstances). (Petition 20.)

Although *U.S. v. Owens*, 902 F.2d 1154, 1155 (4th Cir. 1990) (Opp. 10) states that timeliness is an element of § 455 recusal, it provides no guidance on how to evaluate timeliness, thus leaving the state of the law in doubt. Similarly, in *Travelers Ins. Co. v. Liljeberg Enterprises, Inc.*, 38 F.3d 1404, 1410 (5th Cir. 1994) (Opp. 10, 15), the court notes that a movant must act at the earliest moment after knowledge of the disqualifying facts, but gives no guidance as how to determine that moment. Accordingly, *Travelers* does not undercut *Andrade v. Chojnacki*, 338 F.3d 448, 455 (5th Cir. 2003) (timeliness must be evaluated in context of entire course of judicial proceeding). (Petition 20.)

Whatever else might be said about *Schurz Communications, Inc. v. F.C.C.*, 982 F.2d 1057 (7th Cir. 1992) and *Edgar v. K.L.*, 93 F.3d 256 (7th Cir. 1996) (Opp. 10, 12), they underscore that the state of the law in the Seventh Circuit is in doubt. (Petition 6, 21-23.) *Schurz* questions the validity of *SCA*, 557 F.2d at 117, and *Edgar* holds that, although delay can be fatal, the passage of time is not conclusive if there exists a compelling justification for disqualification. 93 F.3d at 257. Neither *Schurz* nor *Edgar* overrules *SCA*.

The recognition in *Preston v. U.S.*, 923 F.2d 731 (9th Cir. 1991), that there is no *per se* rule, but recusal should be sought with reasonable promptness, and the similar observation in *Skokomish Indian Tribe v. U.S.*, 410 F.3d 506 (9th Cir. 2005), illustrate that the state of the law in the Ninth Circuit is uncertain. Neither makes reference to *In re*

Manoa Finance Co., 781 F.2d 1370 (9th Cir. 1986) (§ 455 imposes self-enforcing judicial obligation; failure to move for recusal below does not preclude raising issue on appeal). Thus, *Manoa* strongly suggests that timeliness is not dispositive.

Although the court in *U.S. v. Pearson*, 203 F.3d 1243, 1276 (10th Cir. 2000) observes that promptly filed recusal motions conserve resources and serve justice, it also notes it had not attempted to define the moment such motions become untimely, leaving uncertain the factors to be considered. Likewise, in *U.S. v. Slay*, 714 F.2d 1093 (11th Cir. 1983) (Opp. 11), the court writes that a recusal motion must be timely, but provides no guidance on what to consider in making the determination, again leaving the law uncertain. Finally, the holding in *U.S. v. Barrett*, 111 F.3d 947, 951 (D.C. Cir. 1997) (Opp. 11), that failure to move for recusal below forecloses consideration of the issue on appeal places that opinion directly at odds with the Ninth Circuit's opinion in *In re Manoa Finance Co., supra.*

In summary, the cases cited establish that, as Respondent concedes, the circuits have produced various formulations of the timeliness rule. In short, the state of the law in some circuits is in doubt; and, the Eighth Circuit stands alone in its position that timeliness – the mere passage of time – is the be all and end all of recusal analysis.

D. Full Record Denied. Before the bankruptcy judge issued his 117-page opinion, Petitioner

had no discovery, no input into the "record," and no opportunity to brief or argue the issue. The bankruptcy court issued its decision solely on the basis of the record it created, the Respondent's self-serving affidavit, (Petition 14-15), with no input from Petitioner, except its Recusal Motion. (App. 221-63.)

Respondent does not deny that Petitioner was denied a full record. Indeed, Respondent concedes that *Moran v. Clarke*, 296 F.3d 638 (8th Cir. 2002) requires the evaluation of a recusal motion in light of all the relevant facts. (Opp. 20.) It is axiomatic that there can be no such evaluation in the absence of a full record. Such record is also mandatory under the holding of this Court in *Sao Paulo,* requiring consideration from the perspective of "a reasonable person, knowing all the circumstances." 535 U.S. at 232. That Petitioner was entitled to make a full record on the merits is unassailablele. It was an abuse of discretion – if not also a denial of procedural due process – for the bankruptcy judge to deny Petitioner such opportunity.[1]

E. Diversionary Tactics. One motive for recharacterizing the issues is transparent: Respondent desires a platform from which to bombard

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[1] Respondent misses the point in citing *In re Federal Skywalk Cases*, 680 F.2d 1175 (8th Cir. 1982). (Opp. 20.) Petitioner cited *Skywalk* not to establish that discovery is always required, but as requiring a full record. (Petition 37.) *Accord Little Rock School Dist. v. Pulaski County Special School Dist. No. 1*, 839 F.2d 1296, 1302 (8th Cir. 1988). *See also* Petition 37.

Petitioner with a litany of allegations, all calculated to discredit Petitioner and distract this Court. Respondent's allegations are irrelevant, unsupportable, and false or misleading. Among the most egregious are:

> **1. No Tactical Recusal.** Respondent, arguing the filing of the Recusal Motion was tactical, states: "The ink on the [June 13, 2006] order [approving compromise of Petitioner's claim] was barely dry when [Petitioner] filed a motion for recusal on June 29, 2006. . . . " (Opp. 4.) The fact omitted is that, prior to the entry of that June 13 order, Petitioner's counsel had announced in open court that:
>
> > [Petitioner] was preparing a motion asking the Court to recuse itself. [Counsel] explained he was making the announcement to avoid "sandbagging" complaints and because he did not want to wait to make the announcement until it was known whether it would get a favorable ruling on the proposed settlement.
>
> (App. 142.) Counsel's disclosure defeats any claim of bad faith tactics.
>
> The foregoing is the only specific instance Respondent identifies as an attempt by Petitioner to use its Recusal Motion as a tactic. Respondent has identified no other instances to show that the motion was filed to gain tactical advantage – nor could he; there was none.

2. No Bad Faith. Respondent attempts to manufacture an issue of bad faith under *Chambers v. NASCO Inc.*, 501 U.S. 32 (1991). (Opp. 7.) The contention that bad faith was at issue in this case is not sustainable.

Here, the bankruptcy court denied the Recusal Motion on the merits under § 455 and as untimely. (App. 193-94.) Nowhere did it find the Motion was filed in bad faith. The district court, although gratuitously making a "finding" of bad faith,[2] (App. 34), merely affirmed the order of the bankruptcy court. (App. 35, 62.) The Eighth Circuit made no finding of bad faith. It found the Recusal Motion "untimely" and, on that "basis alone,"

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[2] Such "finding" was based, *inter alia*, upon the trustee's self-serving and uncrossed affidavit, the bankruptcy court's 117-page selective, incomplete, and sometime incorrect opinion (*see* App. 20, 36), and the district judge's personal opinion of the reputation of the trustee. (App. 22.) The district judge speculatively opined that the reporter's affidavit (App. 255) was drafted by Petitioner's counsel (App. 21) (*but cf.* finding in related proceeding (*see* App. 36) by U.S. Attorney that content of reporter's affidavit "was written solely by her"). The district judge also assailed such affidavit as "scandalous," containing "opinions and conclusions rather than facts," (App. 22) as does Respondent. (Opp. 18.) If the reporter's affidavit suffers from such infirmities, then likewise do the trustee's affidavit and certain portions of the bankruptcy court's and district court's opinions. In calling the affidavit "scandalous," not only did the district judge do so without supporting evidence, he misapprehended the meaning of "scandalous." *See In re Neal*, 461 F.3d 1048, 1053-54 (8th Cir. 2006) ("scandalous" means more than injury to reputation).

affirmed the "district court's decision to affirm the bankruptcy court's denial of the [Recusal Motion]. . . . " (App. 6-7.)

Respondent makes the unremarkable statement that under *Chambers*, "[c]ourts have the inherent power to prevent and sanction bad-faith conduct." (Opp. 7.) Respondent's *non sequitur* is: "The Eighth Circuit's timeliness rule prevents bad faith." *Id.* To the contrary, the Eighth Circuit's timeliness doctrine (based on the mere passage of time) bars review on the merits, precluding even the finding of good or bad faith.

Respondent's Opposition, contrived on the false premise of bad faith, must be rejected as a cynical attempt to distract this Court from the critical national issue at hand – public confidence in the federal judiciary.

3. Petitioner Claimed Motion Timely. Respondent falsely states: "[Petitioner] has not claimed its motion was timely." (Opp. 9.) Petitioner has always claimed the motion timely, based on a pattern of rulings and course of conduct, starting in July 2004 with the conversion from Chapter 11 to Chapter 7, which pattern continued to unfold over time, through a key hearing on May 4, 2006, when the bankruptcy judge revealed the extent and continuing nature of his bias. (Petition 9-10.)

In May 2006, the reporter, having written articles about the ethanol plant for over

seven years (App. 255) and clearly concerned about the bias she had observed, agreed to write the affidavit (App. 262) which was attached to the Recusal Motion. (App. 221-263.) She signed the affidavit on June 12, 2006, and the Recusal Motion was filed on June 29, 2006. *Id.*[3]

This pattern and course of conduct was detailed in the Recusal Motion (App. 221-254), briefs to the district court (*see, e.g.*, App. 264-335), and in over 5 pages of the Reply Brief to the Eighth Circuit. But those courts refused to consider that, under the circumstances – especially in the context of a bankruptcy case, consisting of numerous contested matters and adversary proceedings – timeliness should be gauged over the sequence of accumulated events, with time to start running only at the last event.

Petitioner filed as soon as it was reasonably convinced the motion was meritorious. (*See* Petition 27.) However, the Eighth Circuit's *sui generis* timeliness doctrine precluded consideration of the pattern and course of conduct.

4. Good Faith in Retrofitting Plant. Respondent attempts to create the false impression that Petitioner deliberately violated

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[3] The reporter's affidavit includes evidence of bias based on extrajudicial source and on violations of judicial ethics. (Petition 33-35.)

a bankruptcy court order in retrofitting the plant without authorization. (Opp. 2-4.) The true facts are set out in the Petition at 8-9. Respondent ignores that even without authorization, Petitioner's entire claim was entitled to administrative expense priority. This is so because under 11 U.S.C. § 503(b)(1)(A) Petitioner's expenditure was an actual and necessary cost of preserving the estate, *In re Bellanca Aircraft Corp.*, 850 F.2d 1275, 1284-85 (8th Cir. 1988), and under § 503(b)(3)(D) resulted in a substantial contribution to the Chapter 11 case. *In re Cellular 101, Inc.*, 377 F.3d 1092, 1095-97 (9th Cir. 2004). (Petition 9.)

5. Other Diversions. Respondent implies Petitioner surrendered its recusal rights by failing to appeal adverse decisions. This is nonsensical. The district court and Eighth Circuit records show Petitioner took appeals when in its best interests.

Respondent states that the district court struck Petitioner's brief because it was "overlength" and "scandalous." (Opp. 5.) The brief was 49 pages, (App. 264-335), within the 50-page limit of Fed.R.Bankr.P. 8010(c).

Respondent implies that Petitioner's attorney authored the "under the thumb" and "kangaroo court" statements in such brief. (Opp. 5.) As Respondent well knows, these descriptions were direct quotations from the reporter's affidavit (App. 261); the words were hers (n.2, *supra*); and they were

repeated only as hers. (App. 292-93.) The affidavit was essential to Petitioner's meeting the § 455(a) standard of whether a "judge's impartiality might reasonably be questioned by the average person . . . who knows all the relevant facts of a case." *Moran v. Clarke*, 296 F.3d 638, 648 (8th Cir. 2002).[4]

In attempting to discredit Petitioner, Respondent takes issue with which bankruptcy judge denied discovery. (Opp. 6.) Judge Kressel, in Minnesota, did sign the order – approximately one hour after Judge Hoyt, in South Dakota, referred the matter to him by electronic order. As set fourth previously, Petitioner's complaint is that discovery was unfairly denied, regardless of which bankruptcy judge signed the order.

F. Waiver and Forfeiture. Respondent misunderstands Petitioner's waiver/forfeiture argument. The Eighth Circuit's timeliness doctrine of necessity derives from a waiver or forfeiture theory – as such was the operative consequence to Petitioner. This Court has noted, "[n]o procedural principle is more familiar . . . than that a . . . right . . . may be forfeited . . . by the failure to make timely assertion of the right before a tribunal having jurisdiction to determine it." *U.S. v. Olano*, 507 U.S. 725, 731 (1993) (internal quotation marks omitted). Moreover, "[a]

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[4] As to whether the brief is "scandalous," given Petitioner's high burden of proof, the brief is submitted in its entirety at App. 264-335.

right that cannot be waived cannot be forfeited by other means. . . . " *Freytag v. C.I.R.*, 501 U.S. 868, 894 n.2 (1991) (Scalia, J., concurring). Significantly, waiver is forbidden under § 455(b) and conditionally forbidden under § 455(a). *See* § 455(e) (App. 200).

The opinion below applies the timeliness doctrine as a prophylactic rule, rendering Respondent literally correct that "[t]his case does not present an issue of waiver or forfeiture, but of untimeliness." (Opp. 17.) However, that is precisely the point – the timeliness doctrine is not made of whole cloth.

Questions as to the import of timeliness in § 455 analysis arise regularly in federal courts. Further guidance from this Court is necessary, as the disposition of recusal motions have a serious impact on public perception of the integrity of the judiciary. The need for plenary review is self-evident.

CONCLUSION

The Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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November 4, 2008

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF SOUTH DAKOTA
NORTHERN DIVISION

IN RE:

TRI-STATE ETHANOL COMPANY, LLC,

Debtor.

Case No. BK 03-10194
Chapter 11

MOTION FOR RECUSAL

(Filed June 29, 2006)

COMES NOW Tri-State Financial, LLC, ("TSF") a creditor of Tri-State Ethanol Company ("TSE") and holder of an equity interest in TSE, in this case, and respectfully moves that the Honorable Irvin Hoyt, United States Bankruptcy Judge, to whom this bankruptcy case has been referred, recuse himself or that he be disqualified from presiding over any and all proceedings in this bankruptcy case in which TSF has or will have an interest in the future. In support of this motion, TSF shows the Court:

I.

1.1 This Motion is brought under:

(a) 28 U.S.C. §455(a);

(b) the doctrine enunciated in *United States v. Pfizer Inc.*, 560 F.2d 319 (8th Cir. 1977);

(c) 28 U.S.C. §455(b); and

(d) the Due Process Clauses(s) of the United States Constitution.

II.

2.1 There are major unresolved disputes in this case between the Trustee, TSF and North Central Construction Company Inc. ("NCC")

2.2 NCC is the general contractor that built TSE's ethanol plant ("Ethanol Plant"). NCC's owner was also in the position of a fiduciary as a member on and sometimes president of TSE's Board of Managers. NCC claims cost overruns of approximately 3.5 million. The Ethanol Plant did not work and produce ethanol as it was supposed to do. The major disputes between the Trustee, TSF and NCC, include whether TSF's objections to NCC's claim should be sustained and NCC's claim should be disallowed in whole or in part, on grounds which in summary include: (i) material breaches by NCC of its fiduciary duties owed to TSE; (ii) material breaches by NCC of its express contractual obligations (including warranties) owed to TSE; (iii) material breaches by NCC of its implied contractual obligations (including its duty of good faith and fair dealing and warranties); and (iv) whether NCC's claim should be offset in whole or in part by counter claim(s) for damages to TSE caused by any or all of the material breaches alleged in (i), (ii) and (iii) above or by partial breaches; (v) whether NCC is entitled to share in the increase in the value of the reconstructed Ethanol Plant that resulted from improvements made and/or increased market value after May 23, 2003; and (vi) whether any claim of NCC that is owed should be equitably subordinated to TSF's claim and/or other claims in adversary

proceeding No. 05-01009 which TSF brought against NCC and the Trustee; and (vii) whether the Trustee's proposed compromise with NCC with respect to NCC's claim is in the best interest of the estate; and (viii) whether any compromise between the Trustee and NCC is or should be binding has binding on TSF.

2.3 There are also major disputes in this case between the Trustee, TSF, and Murphy Brothers.

2.4 The major disputes between the Trustee, TSF, and Murphy Brothers, include (i) whether TSF's objections to Murphy Brothers claim should be sustained and the claim of Murphy Brothers should be allowed in whole or in part; and (ii) whether the Trustee's proposed compromise with Murphy Brothers is in the best interests of the estate and should be sustained.

2.5 There is also a major dispute in this case between the Trustee and TSF and First Dakota National Bank over whether First Dakota Natural [sic] Bank's claim for a prepayment penalty should be allowed.

2.6 There is also a potential major dispute in this case between TSF and the Trustee over whether the Trustee properly performed his fiduciary duties owed to TSF and over the amount of the compensation to which the Trustee may be entitled.

2.7 There are also other disputes in this case between the Trustee and TSF over the allowance of other claims.

2.8 TSF, as the holder of an allowed subordinated unsecured claim in the amount of $1,190,000 and as the holder of an equity interest in TSE, has a financial stake in the outcome of the above disputes and all disputes with all creditors.

III.

3.1 28 U.S.C. §455(a) provides a judge "shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned."

3.2 *United States v. Pfizer Inc.*, 560 F.2d 319, 322-23 (8th Cir. 1977) holds that a judge sitting as a trier of fact who has played an active and aggressive role in settlement and expressed strong opinions on the legal and factual issues of the cases creates an impression of bias; and, if the judge then assumes a fact finding function may erode the right of a litigant to obtain a fair trial in fact as well as in appearance. *See also Alexander v. Primerica Holdings, Inc.*, 10 F.3d 155, 163, 166 (3rd Cir. 1993).

3.3 The disqualification in §455(a) is designed to promote public confidence in the integrity of the judicial process by replacing the subjective standard that was in the statute before 1970 with an objective test. *Liteky v. United States*, 510 U.S. 540, 548 (1994); *Moran v. Clarke*, 296 F.3d 638, 648 (8th Cir. 2002) (*en banc*).

3.4 "By enacting section 455(a), Congress sought to eradicate not only actual, but also by the

appearance of impropriety in the federal judiciary." *Moran v. Clarke*, 296 F.3d 638, 648 (8th Cir. 2002) (*en banc*).

3.5 Under §455(a), actual bias is irrelevant. *Moran v. Clarke*, 296 F.3d 638, 648 (8th Cir. 2002) (*en banc*).

3.6 The Eighth Circuit Court of Appeals has recast the issue under §455(a) to be "[w]hether the judge's impartiality might reasonably be questioned by the average person on the street who knows all of the relevant facts." *In re Kansas Public Retirement System,* 85 F.3d 1353, 1358 (8th Cir. 1996).

3.7 The inquiry under §455(a) about a judge's impartiality, including as it does "all the relevant facts", therefore, warrants consideration of Judge Hoyt's course or pattern of rulings and his course of conduct. *Moran v. Clarke*, 296 F.3d 638, 649 (8th Cir. 2002) (*en banc*).

3.8 The doctrine enunciated in *States v. Pfizer, Inc., supra*, not only prohibits a judge sitting as a trier of fact from expressing strong views about the legal or factual issues in the case at any time before the trial is over, but also mandates that the judge avoid even recommending an actual settlement before or during trial because "a fundamental principle of justice" is that "[i]t is important that a litigant not only receive justice, but that he believe he has received justice." 560 F.2d at 323.

3.9 "[w]here the question is close, the judge must recuse himself". *Union Planters Bank v. L & J Development Company, Inc.*, 115 F.3d 378, 383 (6th Cir. 1997).

IV.

4.1 It is respectfully submitted that the average person on the street who knows all the relevant facts would conclude that as provided in §455(a), Judge Hoyt's impartiality toward TSF might reasonably be questioned. There are six bases on which such a fully informed average person on the street might reasonably question Judge Hoyt's impartiality. Each by itself is sufficient for recusal as is any combination of two or more.

Basis For Bias #1

4.2 Central to the appearance of Judge Hoyt's bias against TSF is his insuppressible conviction that TSF in general and its Omaha members ("Omaha Group")[1] in particular thumbed their noses at his judicial authority, abused the bankruptcy process, and nefariously schemed to get control of the debtor, Tri-State Ethanol Company, LLC ("TSE"). Implicit though unmistakable in such conviction of Judge

[1] The Omaha Group is comprised of approximately 30 individuals, including John Hoich, Jim Jandrain, and Randy Kramer.

Hoyt is that TSF and the Omaha Group throughout this case should be punished economically in ways designed by him for their bad behavior, particularly for abusing the bankruptcy process.

4.3 The parties that Judge Hoyt strongly believes were associated with the abuse of the bankruptcy process and schemed to get control of TSE are TSF (including the Omaha Group) and ICM. They are the parties that were connected to the re-engineering and reconstruction ("Retrofitting") of TSE's Ethanol Plant during TSE's Chapter 11 case.

4.4 On July 28, 2004, Judge Hoyt gratuitously denounced those associated with Retrofitting TSE's Ethanol Plant during TSE's Chapter 11 case. His denunciation was made in the course of the hearing in which Judge Hoyt announced his decision to convert TSE's Chapter 11 case to a Chapter 7 case. Judge Hoyt's denunciation, from which he has never receded, shows he has a closed mind on whether those associated with such Retrofitting disregarded his judicial authority, abused the bankruptcy process, and put into action a nefarious scheme to get control of TSE:

> " . . . what the approach has been in this case [is] it's better to get forgiveness than permission, cause all of these things, as you well know required permission. And when permission was refused initially, then they just went off and did it and said we'll see if we can get forgiveness when it comes time for confirmation. . . ."

72:10-15

"So what we, what we engaged in is we engaged in a plan to significantly expand the plan [sic] and eventually, the way this was structured, there would be a new equity group created and the old equity group would go away. That's what was going to happen if, if there had been a confirmation."

76:12-16

Some? A lot. And that meant the contributions that have been given before, whereas it's going to be lost in the, in the, in the shuffle, number one. There would be a different group of control, number two. And it was an entirely different game, wasn't it?"

76:19-23

"Well, I'm, I'm – what I'm saying is that the plant was at – was apparently able to operate as it was originally intended, whether that was an inefficient or efficient we don't know for sure. . . ."

77:1-4

" – prior that it was an inefficient operation and needed to be brought up to seventeen to eighteen to twenty million gallons and, everything would be great. I had never heard before today that we were on the doorstep of having this thing ready to go. And what really has taken place here was the, the use of the bankruptcy process to infuse money into this and in essence – and, and it was –

and in what – what in essence was going to happen was going to be a change of control, and I'm picking on the wrong person. I shoot my arrow in the wrong direction."

77:6-15

" . . . from what I've seen it would be very hard to call this a good faith filing . . . "

89:17-18

4.5 The backdrop of Judge Hoyt's gratuitous denunciation is a motion filed on September 25, 2003, by TSE ("TSE's Motion"), then a Debtor in Possession in a Chapter 11 case, for approval of a multi-faceted Stipulation between TSE, TSF, and First Dakota National Bank ("FDNB") ("9/25/03 Stipulation"). By TSE's Motion and the 9/25/03 Stipulation, TSE sought authorization: to enter into a contract with ICM for Retrofitting TSE's Ethanol Plant; to incur debt consisting of loans from TSF and FDNB to pay for the Retrofitting; for such loans to be entitled to super priority over other expenses of administration and be secured by a post-petition priming first lien on all assets of TSE; for approval of TSE's use of cash collateral in which FDNB had an interest; for TSF and FDNB to have the right of an advance approval of expenditures by TSE for Retrofitting and startup costs; and for the treatment by TSE of FDNB in a then yet-to-be-filed Chapter 11 plan.

4.6 Before any decision by Judge Hoyt on the 9/25/03 Motion. on advice of former Omaha counsel and South Dakota counsel, TSE and ICM, with

assistance from TSF and the Omaha Group, had begun to Retrofit the Ethanol Plant, because the contractor, ICM, had significant work commencing in early 2004 and would not be able to perform the work at Tri-State if they deferred the starting date. Gaylor and NCC had constructed similar plants in Galva, IA, and Sioux Center, IA, both of which also did not work. ICM was involved in both of those retrofits. Both plants are now successfully running significantly over their design capacity due to the retrofit. ICM was so confident that the Tri-State plant would run after being retrofitted and, being familiar with the inadequacies of NCC and Gaylor Engineering and related hardships they caused the industry and those communities, that Dave VanderGriend (President/Owner of ICM), knowing the plant was in bankruptcy, agreed to perform the retrofit for only a guarantee of payment of $1,190,000 so they could purchase the necessary equipment needed for the retrofit, including a new boiler and stainless steel tanks to replace the already corroded carbon steel tanks.

4.7 By decision and order on December 12, 2003, Judge Hoyt denied TSE's Motion in all respects ("12/12/03 Decision") and ("12/12/03 Order").

4.8 When Judge Hoyt denied TSE's Motion by the 12/12/03 Decision and the 12/12/03 Order, TSE, ICM, and TSF, again on the advice of former Omaha counsel, without objection of TSE's South Dakota counsel, continued to Retrofit the Ethanol Plant. They did so without TSE making any contract with ICM; without any super priority for loans by TSF and

FDNB ahead of other administrative expenses, and without any post-petition priming first lien on TSE's assets for any loan. They also did so to protect and preserve TSE's estate, mainly the going concern value of TSE's Ethanol Plant. In the process of Retrofitting, ICM increased the name plate capacity of the Ethanol Plant from 14 MGY to 20 MGY. As mentioned in 4.6 above, ICM had successfully retrofitted ethanol plants in Galva, Iowa, and Sioux Center, Iowa, and, in the process, ICM had increased their nameplate capacities. One (or both) of those plants was a "cookie cutter" plant for TSE's Ethanol Plant.

4.9 It is respectfully submitted that the gratuitous denunciation of those associated with the Retrofitting of the Ethanol Plant by Judge Hoyt on July 28, 2004, and the "facts" Judge Hoyt states that are quoted above in paragraph 4.4 are not facts and are not supported by credible evidence.

4.10 One can only ponder why Judge Hoyt was not objective, impartial, or fair in what he said and did not say on July 28, 2004; why Judge Hoyt did not acknowledge that he knew of the ongoing Retrofitting of the Ethanol Plant; that the Retrofitting was on a voluntary basis without contract; that he also knew that TSF was loaning TSE money to facilitate the Retrofitting of the Ethanol Plant; that he never ordered TSF, ICM, or TSF to stop Retrofitting; that the ongoing Retrofitting had been fully disclosed in TSE's February 17 Amended Disclosure Statement which Judge Hoyt had approved; and that as Judge Hoyt was accusing parties of a scheme to increase

control of TSE there was on file a Modified Plan of Reorganization that TSE had filed on June 24, 2004, which with respect to equity in summary provided that: holders of equity interests in TSE would retain the equity interests they held on May 23, 2003, when TSE filed Chapter 11; new investments of approximately $3.5 million would be required to pay for the initial Retrofitting and the startup of the Ethanol Plant; and that all holders of equity interests on May 23, 2003, had the right to make new investments toward the $3.5 million in amounts necessary for such holders to keep the same percentage of ownership in TSE as they held before May 23, 2003.

4.11 Judge Hoyt appears to have a closed mind against TSF and does not allow for any possibility that, contrary to his expressed views, the evidence, if the disputes listed in part II would go to trial, would establish any of the following:

> A. Since the Retrofitting of the Ethanol Plant was accomplished without any contract between TSE and ICM, without any management contract between TSE and United BioEnergy, without any super priority or other liens on TSE's assets, and without many of the attributes of a Chapter 11 plan included in the 09/25/04 Stipulation and Agreement, the Retrofitting was not an abuse of the bankruptcy process; and it was reasonable for the parties to follow the advice of their former counsel. The decisions were all made to preserve the assets of the

business and continue in the business of producing ethanol.

B. There was no nefarious scheme orchestrated by TSF or anyone to increase control of TSF.

C. The increase of the nameplate capacity of the Ethanol Plant from 14 MGY to 20 MGY was done for reasons of prudent engineering, cost effectiveness and profitability and was not orchestrated by the Omaha Group or any of its members. Much of the increase in capacity was the direct result of efficient operation and repair or replacement of what already existed, not expansion of the facility.

D. The loans that TSF offered to make and made were offered and made for the legitimate reasons that there was no other source of credit and not as part of any nefarious scheme.

E. The Retrofitting of TSE's Ethanol Plant was done to preserve the going concern value of TSE's Ethanol Plant.

F. A judge other than Judge Hoyt should preside over and resolve any claims that TSF violated Judge Hoyt's order; and another judge should also preside over and decide any and all contested matters and adversary proceedings to which TSF is a party or in which TSF should have an interest.

G. The appearance that Judge Hoyt might not be impartial toward TSF is so pervasive in South Dakota that the other judge referred to in paragraph F should be a bankruptcy judge from another state such as Iowa.

Basis For Bias #2

4.12 A fully informed person on the street might reasonably also doubt Judge Hoyt's impartiality because he appears to have a deep seated dislike for, distrust of, and antagonism toward TSF and certain members from the Omaha Group who are important witnesses in the disputes listed above in part II.

4.13 Attached hereto as Exhibit A is a copy of an affidavit of Grace ("Mimi") Larsen. In her Affidavit, Larsen recounts her private October 26, 2004, conversation with Judge Hoyt following the Chapter 7 sale of the Ethanol Plant in Judge Hoyt's courtroom. Judge Hoyt had presided over the sale.

4.14 As shown by the Larsen Affidavit, Judge Hoyt strongly dislikes and is antagonistic toward John Hoich, a member of TSF and the Omaha Group,[2] apparently because: in Hoich's testimony as a witness in support of TSE's 9/25/03 Motion on October 22, 2003, Hoich testified that he had a net worth of $25

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[2] Larsen's Affidavit indicates considerably more than Judge Hoyt's dislike of and antagonist [sic] toward John Hoich.

million to $30 million and had the ability by himself to pay to Retrofit the Ethanol Plant; Hoich was instrumental in causing Dave VanderGriend to become involved with TSE and causing ICM to Retrofit the Ethanol Plant during TSE's Chapter 11 case, expanding its nameplate capacity from 14 MGY to 20 MGY; Judge Hoyt heard in testimony on July 28, 2004, that Hoich had provided $900,000 to ICM to buy equipment installed in the Ethanol Plant during the Chapter 11 Retrofitting; or because Judge Hoyt believes that Hoich "hit on" his clerk. As we know from Larsen's Affidavit, Judge Hoyt experienced and expressed pleasure in seeing Hoich "sweat" in the public auction of the Ethanol Plant on October 26, 2004, during which TSF lost out in its attempt to buy the Ethanol Plant.

4.15 Judge Hoyt also appears to have a strong dislike for and distrust of James Jandrain, a CPA, the organizing member of the Omaha Group and a member of TSF. This dislike probably originated in Jandrain's testimony as a witness in support of TSE's 9/23/03 Motion on October 22, 2003, and also may be associated with Judge Hoyt's knowledge that Jandrain, along with Hoich, was instrumental in causing Dave VanderGriend to become involved with TSE, and through ICM, Retrofit the Ethanol Plant, expanding its capacity from 14 MGY to 20 MGY in the process.

4.16 Judge Hoyt has implicitly, if not explicitly, accused important witnesses associated with TSF and

the Omaha Group of not being truthful. In the hearing held on October 22, 2003, on TSE's 9/25/03 Motion to approve the 9/25/03 Stipulation and Agreement between TSE, TSF, and FDNB, Judge Hoyt, without evidence to the contrary, chose to disbelieve the testimony of Hoich, Jandrain, and Randy Kramer, the testimony of Dave VanderGriend, who then had successfully retrofitted 15 ethanol plants, and the testimony of Daniel Swanda, loan officer of FDNB, to whom TSE owed more than $9 million, approximately half of TSE's total debt. With respect to two members of the Omaha Group, James Jandrain and Randy Kramer, Judge Hoyt also impugned their motives. He decided that the 9/25/03 Stipulation and Agreement was "tainted" because it involved the Omaha Group who were insiders and provided a "hold" on litigation brought by FDNB on personal guarantees by Jandrain and Randy Kramer of a $600,000 operating note to FDNB from TSE.

4.17 As shown by the Larsen Affidavit, when TSF retained the services of Jerrold L. Strasheim, who formerly was a referee in bankruptcy and bankruptcy judge in Nebraska, Judge Hoyt without any basis concluded that the motivation of TSF was to improperly influence Judge Hoyt in that Judge Hoyt and Strasheim would have a "good old boy" relationship. Judge Hoyt decided to show Strasheim that would not work, apparently by converting TSE's Chapter 11 case to Chapter 7.

4.18 Based on Judge Hoyt's dislike, distrust, and antagonism toward TSF and its members, and

possibly its attorney, a fully informed person might reasonably doubt that Judge Hoyt could bring himself to do justice with respect to TSF, particularly when there is added Judge Hoyt's apparent punishments described below in #3.

Basis For Bias
#3

4.19 Another basis on which a fully informed person on the street might reasonably doubt Judge Hoyt's impartiality toward TSF is the pattern of Judge Hoyt's rulings which have given every appearance of being improperly vindictive, punitive or both.

4.20 The decision of Judge Hoyt on July 28, 2004, to convert TSE's Chapter 11 case to Chapter 7, itself appears to target TSE, TSF, and the Omaha Group, and be vindictive or punitive mainly for what Judge Hoyt had decided was disregard of his judicial authority, but also perhaps for what he had decided was a scheme and also perhaps, as suggested by the Larsen affidavit, to put or keep Strasheim in his place. This is a more likely explanation than his discussion on July 28, 2004, of Chapter 11 confirmation standards.

4.21 When Judge Hoyt converted TSF's case from Chapter 11 to Chapter 7, he appears to also be punishing TSF for not agreeing on the terms of a written settlement agreement with NCC and the Trustee. It had been recited in court on June 21, 2004, that TSF and NCC would enter into a written

settlement agreement. It was agreed that the terms of that written settlement agreement were supposed to include that TSF would pay NCC $2.5 million, $1 million of which was for an assignment of NCC's equity interest in TSE, $1.5 million of which was for an assignment of NCC's claim, and all of which was to eliminate NCC's objection to confirmation of TSE's plan. TSE had agreed to file a plan under the terms of which NCC's disputed claim being assigned to TSF would be allowed as a secured claim for $1.5 million. The dispute between NCC and TSF, and why no written agreement had been signed, was whether confirmation of TSE's plan was a condition precedent to the settlement. Because North Central had raised an issue as to whether TSF had the ability to pay the $2.5 million, TSF had collected $2.5 million from certain of its members in the Omaha Group. The $2.5 million had been placed in Strasheim's firm's trust account in Omaha to be paid if and when a written agreement was signed and TSE's Chapter 11 plan was confirmed by final order. Judge Hoyt encouraged Strasheim to agree on behalf of TSF that confirmation of TSF's Chapter 11 plan was not a condition of the settlement and for TSF to agree to pay the $2.5 million whether or not there was confirmation of TSE's yet to be filed plan. Yet the next day, on July 28, 2004, Judge Hoyt disclosed that because of his independent duty to apply confirmation standards, whether there were objections to confirmation or not, he would never have confirmed TSF's Chapter 11 plan. Thus, on July 28, 2004, Judge Hoyt had attempted to influence Strasheim and TSF to agree to

pay $2.5 million to NCC in a case that he was certain would be a chapter 7 case. TSF would have been agreeing to pay $1 million for equity and $1.5 million for a claim which, absent TSE's agreed treatment in a Chapter 11 plan, would be a disputed claim. It is not reasonable to characterize Judge Hoyt's behavior on July 28, 2004, in attempting to influence TSF to agree to pay $1 million for equity while not disclosing to all parties that of TSE's Chapter 11 plan could not be confirmed, as behavior that is objective, fair, and impartial.

4.22 ICM did the Retrofitting of TSE's Ethanol Plant in TSE's Chapter 11 case. Judge Hoyt appears to have punished ICM for Retrofitting the Ethanol Plant by relegating ICM's $2.3 million claim for the Retrofitting to general unsecured status when ICM was entitled to Chapter 11 priority status.

4.23 TSF and the Omaha Group were, of course, also associated with the Retrofitting of the Ethanol Plant in TSE's Chapter 11 case. Judge Hoyt appears to have punished TSF for involvement in the Retrofitting by comments putting TSF's right to payment of Chapter 11 administrative expenses at risk. On January 24, 2004, TSF had filed a request for payment of Chapter 11 administrative expenses in the amount of $1,983,654 and a contingent, duplicating proof of claim for the same amount. Judge Hoyt's closed mind, described above in paragraph 4.4 and events such as those described below in paragraphs 4.32 and 4.33, forced TSF to settle TSF's request for Chapter 11 administrative expense in the amount of

$1,983,654.42 with the Trustee. The settlement was entered into on May 4, 2005, before an evidentiary hearing on TSF's request for Chapter 11 administrative expenses was to start. Under the terms of the settlement, TSF agreed that the $1,190,000, which TSF advanced for equipment ICM installed in TSE's Ethanol Plant would be allowed as a general unsecured claim rather than a Chapter 11 Administrative Claim and subordinated to other allowed general unsecured claims. As indicated below in paragraph 4.36 and as appears from the Larsen affidavit, Judge Hoyt appears to control which claims the Trustee objects to and which he does not.

4.24 Although not associated with the Retrofitting of TSE's Ethanol Plant, Kramer is a member of the Omaha Group. Judge Hoyt appears to have punished Randy Kramer for being a member of the Omaha Group. On October 14, 2005, Judge Hoyt sustained the Trustee's objections to the claims of Randy Kramer. Kramer had filed a claim in the amount of $33,350.33. Judge Hoyt disallowed $17,500 on grounds no minutes of TSE's Board of Managers authorized payment for his services, a requirement that Judge Hoyt has yet to apply to other creditors of TSE like NCC. He allowed Kramer's claim in the reduced amount of $15,850.33. Kramer is an important witness for TSF, particularly in its opposition to the claim of NCC.

4.25 Similarly, Judge Hoyt appears to have punished James Jandrain, a major member of the Omaha Group, for being associated with Retrofitting

TSE's Ethanol Plant in TSE's Chapter 11 case. On May 5, 2006, Judge Hoyt sustained Trustee's objections to the claim of James Jandrain filed in the amount of $53,850.33. He disallowed $49,950.33, again on grounds applied only to Jandrain and not to other creditors. He allowed only $3,900. His order is on appeal. As mentioned above, Jandrain is a member of the Omaha Group and an important witness for TSF in all pending litigation.

4.26 And Judge Hoyt appears to have decided that as punishment there should be no return to holders of equity interests in TSE. This is implicit in his withholding of any rulings on TSF's objections to claims and by his rulings on appointment of professionals and allowance of their fees.

4.27 No rule of bankruptcy law is known that permits Judge Hoyt to punish those associated with the Retrofitting of the Plant by the measures described above.

4.28 The objective observer, because of the appearance that Judge Hoyt has been improperly vindictive or punitive in the instances listed above, might reasonably doubt that in the litigation in part II above that Judge Hoyt would be impartial.

Basis For Bias
#4

4.29 The fully informed average person on the street might also reasonably doubt Judge Hoyt's

impartiality based on a pattern of prejudgments, discriminatory, and unfair treatment of TSF as compared to other litigants in the case.

4.30 In the dispute between TSF and NCC discussed at Judge Hoyt's request in his Chambers on July 27, 2004, over whether confirmation of TSE's Chapter 11 plan was a condition of the settlement that was supposed to be reduced to writing, Judge Hoyt blamed TSF. He placed the blame on TSF without considering evidence, including NCC's first draft of the proposed written settlement agreement and the accompanying letter, as well as other evidence.

4.31 After conversion of TSE's case to Chapter 7, when the Trustee moved to establish bidding procedures for the Ethanol Plant, before the auction on October 26, 2004, TSF moved in writing to extend the date after the auction by which the successful bidder would be required to close. That closing date was one week after the auction and the opening bid was approximately $20,000,000. The logical reason was that to close the loan financing by any party would take more than a week. TSF offered to pay additional costs of the Trustee in holding the Ethanol Plant if TSF were the successful bidder. TSF's motion was summarily denied. At the auction, other bidders sought the same relief and were granted it.

4.32 Judge Hoyt scheduled a telephonic hearing which was held on March 2, 2005, for argument on whether the Trustee's Objections to TSF's request for payment of Chapter 11 administrative expenses

should be sustained without an evidentiary hearing. Implicit in that action by Judge Hoyt was his unfair predisposition that his 12/12/03 Decision and 12/12/03 Order barred TSF from any relief. No evidence was offered in that telephonic hearing. Afterwards, on March 14, 2005, Judge Hoyt issued a letter ruling that an evidentiary hearing be held but also containing 10 paragraphs from the court's 12/12/03 Decision on TSE's Motion summarizing the contents of the 9/25/03 Stipulation, between TSE, TSF, and FDNB which he had not approved. Implicit in his view is that those provisions from the 12/12/03 ruling would be important if not dispositive as to what he decided later on TSF's request and claim for $1,983,654.42 of administrative expenses. He also listed orders authorizing administrative expenses. Again implicit is that he had already decided those orders were important if not dispositive. In addition, in his March 14, 2005, letter ruling, Judge Hoyt summarized some circumstances concerning ICM's application for payment for Retrofitting the Ethanol Plant for TSE during TSE's Chapter 11 case. ICM was requesting $2,310,552.51 as a Chapter 11 administrative expense. Judge Hoyt recited that ICM's claim had not been allowed as a Chapter 11 administrative claim and was instead downgraded and allowed as a general unsecured claim. In doing these things, Judge Hoyt was becoming a virtual advocate against TSF. Implicit in Judge Hoyt's March 14, 2005, letter ruling is the prejudgment that TSF's request for administrative expenses was not viewed favorably by him.

4.33 In the same March 2, 2005, telephonic hearing, TSF argued that since the Trustee in his Objection was not only objecting but also seeking to equitably subordinate any claim of TSF's that was allowed to other allowed claims, the Trustee was obligated by the plain language of Fed.R.Bankr.P. 7001(8) to file an adversary proceeding, not merely an objection. Judge Hoyt announced that he would require the Trustee to file a complaint starting an adversary proceeding. The Trustee filed the complaint on March 14, 2005. He not only asked to equitably subordinate but to recharacterize TSF's debt as equity. Then without warning or request, on March 23, 2005, Judge Hoyt sua sponte entered an order shortening the time for TSF to file its answer to April 8, 2005, fixing April 22, 2005, as the deadline to complete discovery and scheduling a trial on May 2, 2005, thereby arbitrarily depriving TSF of the benefits of the Federal Rules of Bankruptcy Procedure for adversary proceedings. Later he denied TSF's request for a continuance.

4.34 In considering whether to confirm TSE's modified plan of Reorganization, Judge Hoyt invoked his duty to independently apply confirmation standards. In considering attorneys fees for the Trustee and creditors, Judge Hoyt does not invoke his duty to independently pass on such fees. In both cases, there is likely injury to TSF which is known to Judge Hoyt.

4.35 Judge Hoyt does not appear to employ the same standards for disqualification and compensation of the Trustee's attorneys on conflict of interest as he

does for disqualification of TSF's Omaha attorneys. He does not appear to employ the same standards for determining whether TSE should be punished and whether TSE's South Dakota Attorney should be punished.

4.36 Judge Hoyt appears to keep the Trustee subject to Judge Hoyt's control and not independent. When NCC filed its Motion to Enforce a Mediated Settlement ("NCC's Mediation Motion"), the Trustee, through counsel, filed a Response to that Motion on December 14, 2005. In that Response, the Trustee, through counsel, stated repeatedly, unequivocally, and definitely that no settlement had been reached because the parties had been unable to agree upon certain terms. When the matter came to trial on May 4, 2006, Judge Hoyt became a virtual advocate for NCC and against TSF. His remarks show that Judge Hoyt had, in effect, prejudged the Motion. The Trustee, without any advance notice to TSF, did absolutely nothing in support of his Response that there was no settlement. The change from the position taken by the Trustee's counsel to that in the May 4, 2006, hearing appears to result from the Trustee carrying out Judge Hoyt's will.

4.37 On July 7, 2005, counsel for the Trustee had filed a motion for leave to make Gaylor Engineering a party to the Trustee's litigation in NCC's claim. The logical reason for this is that Gaylor Engineering and NCC can be expected to point the finger at each other for defective engineering and defective construction as the party to blame for the Ethanol Plant

not working as it was supposed to work. On the same day, Judge Hoyt sua sponte denied the Trustee's Motion.

4.38 Based on the pattern of the events described above, under this Basis for Bias #4, a fully-informed person might reasonably question Judge Hoyt's impartiality toward TSF.

Basis For Bias #5

4.39 Another basis on which a fully informed person might reasonably conclude that Judge Hoyt might not be impartial towards TSF is that Judge Hoyt at times appears to have aligned himself with NCC and in favor of NCC.

4.40 Judge Hoyt has yet to question the enforceability, validity or amount of the Claim of NCC or NCC's motives in opposing TSE and TSF every step of the way. NCC's opposition was the major opposition to TSE's plans and to TSE's motion to dismiss its case. Judge Hoyt has indulged NCC in nearly all its tactics of questionable motivation.

4.41 Judge Hoyt's failure to question NCC's claim appear to reflect favoritism for NCC. As Judge Hoyt knows or should know: before TSE filed its Chapter 11 case on May 23, 2003, TSE's Ethanol Plant had never worked as it was supposed to work; TSE, before filing Chapter 11 on May 23, 2003, had paid NCC hundreds of thousands of dollars in excess

of the $8.5 million price in the contract for which NCC had agreed to build the Ethanol Plant; by its claims filed in this bankruptcy, NCC seeks total payment (payments before TSE's Chapter 11 case plus payment from TSE's Chapter 7 Estate) of approximately $12 million on an $8.5 million contract; and Robert (Kim) Buchanan, the president and owner of NCC, had at all times from before and during construction by NCC of the Ethanol Plant, sat on TSE's Board of Managers, occupied a fiduciary position to TSE, and for part of those times, was president of TSE's Board of Managers.

4.42 Judge Hoyt also has appeared to favor NCC procedurally by such things as the scheduling a trial date to decide objections to NCC's claim that make it impossible for the Trustee and TSF to adequately prepare for trial and other similar actions, by unnecessarily scheduling hearings at geographically distant places, and by not ruling, at the Trustee's request, and disputes in which the Trustee and TSF are adversaries

4.43 Judge Hoyt also appears to favor NCC by limiting the scope of litigation against NCC. As mentioned above, when the Trustee filed motion papers to bring Gaylor in as an additional party in the Trustee's litigation opposing NCC's claim, Judge Hoyt sua sponte without waiting for NCC or any other party to oppose the motion papers, denied the motion on the same day it was filed.

4.44 A fully informed person on the street might reasonably doubt Judge Hoyt's impartiality and whether he is not predisposed to favor of NCC.

Basis For Bias
#6

4.45 Another basis for which an ordinary man on the street might reasonably doubt Judge Hoyt's impartiality is his involvement in settlement.

4.46 Judge Hoyt has played an active role in settlement discussions between the Trustee, NCC, and TSF. His involvement has been deep and unquestionable. Judge Hoyt knows virtually every aspect of efforts to reach settlement because of disclosure by NCC, many of which aspects should never have been disclosed to Judge Hoyt as fact finder. The known aspects include offers, amounts, and the like.

4.47 Before November 18, 2005, NCC had, without permission of TSF, sent a letter to Judge Hoyt arguing the parties had reached and [sic] agreement in mediation which TSF should be forced to honor, and enclosed forty pages of materials. One enclosure was a copy of a partial transcript of mediation proceedings including privileged parts (if not all parts are privileged). Also included was a copy of what NCC claimed was the last draft exchanged between parties of their settlement efforts to reduce what had transpired in mediation to writing. Judge Hoyt read the letter and its enclosures. There was no criticism by Judge Hoyt of legal counsel for NCC for

presenting privileged material to Judge Hoyt when they knew, or should have known, not to do so. This is not the same treatment accorded Strasheim in litigation with Murphy Brothers.

4.48 On November 18, 2005, in a telephonic status hearing, Judge Hoyt was also made fully aware by the Trustee and NCC of the detailed settlement discussions, on what the Trustee, NCC and TSF agreed, and on what they disagreed.

4.49 In the telephonic conference on November 18, 2005, Judge Hoyt again blamed TSF for not agreeing to pay $2,500,000 to NCC on July 28, 2004, for NCC's claim and equity in TSE's Chapter 11 case. Judge Hoyt appears to have had no concern that TSF would pay $1 million for equity in a Chapter 7 case and $1.5 million for a disputed claim. This was so even though Judge Hoyt knew on November 18, 2005, that NCC, shortly after July 29, 2004, had filed a lawsuit against TSF seeking to enforce the purported settlement but had done virtually nothing to get the case to progress to trial for two years.

4.50 In the same November 18, 2005 telephonic conference, Judge Hoyt, hearing no evidence, intimated that the failure of the Trustee, NCC, and TSF to settle in 2005 was also the fault of TSF.

4.51 As mentioned in paragraph 4.36, on November 21, 2005, NCC filed NCC's Mediation Motion. Along with NCC's Mediation Motion, NCC again provided Judge Hoyt with a partial transcript of mediation proceedings. TSF repeatedly objected to

NCC providing the information to Judge Hoyt on the basis of privilege under applicable South Dakota law and/or the inadmissibility of settlement discussions to show liability under South Dakota and applicable federal law, but Judge Hoyt overruled TSF's objections each time they were made. Moreover, he read the letter and its enclosures sent to him by NCC before November 18, 2005. At the February 9, 2006, evidentiary hearing on NCC's Mediation Motion, the differences of the parties were again aired and the partial mediation transcript formula received from NCC. Further, recently at an evidentiary hearing on May 4, 2006, the full details were again exposed to Judge Hoyt.

4.52 In the hearing on May 4, 2006, Judge Hoyt offered a strong and critical opinion on what TSF had been asking for in order to settle. Judge Hoyt in that hearing also ominously said that when he retired in August he was going to go on recall status to keep this case, saying "you're going to love this." He added: "I'm going to keep this case. I'm going to finish this case." Judge Hoyt has decided he is the only judicial officer that can hear disputes between the Trustee, NCC, and TSF. He has already ruled there was an oral settlement agreement reached; and TSF then opposed approval of that oral settlement – which TSF contends was never enforceable as a matter of right.

4.53 Given Judge Hoyt's extreme involvement in efforts of the parties to reach a settlement, and given Judge Hoyt's remarks about the basis on which TSF was willing to settle, a fully informed person

might reasonably doubt that the settlement and settlement discussions and Judge Hoyt's previous remarks would be ignored by Judge Hoyt in further litigation, particularly litigation over NCC's claim; such a fully-informed person is more likely to think it foolhardy for any reasonable person to believe that Judge Hoyt would decide objectively, fairly and impartially.

V.

5.1 This Motion is also brought under 28 U.S.C. §455(b).

5.2 28 U.S.C. §455(b) provides in relevant part that a judge "shall also disqualify himself . . . (1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding . . . ".

5.3 Because of the appearance of bias, this case should not require a decision whether Judge Hoyt is actually biased or not.

5.4 However, if required, TSF incorporates by reference herein all of the allegations in part IV above.

5.5 The facts in part IV above show that Judge Hoyt is antagonistic toward TSF, that his antagonism is deep seated, that he has a pervasive bias against TSF that he could not ignore even if he chose to, and an objective, fair, and impartial decision by Judge Hoyt is unlikely, if not impossible.

5.6 The facts in part IV above support favoritism for NCC that makes an objective, fair, and impartial decision by Judge Hoyt in litigation between TSF and NCC unlikely, if not impossible.

5.7 The facts in part IV above show Judge Hoyt's involvement in settlement of disputes involving NCC and TSF is too extreme, is tainted by knowledge of details of settlement that counsel improperly brought before Judge Hoyt and is encumbered by prejudgments, such that Judge Hoyt will not render an objective, fair, and impartial decision in litigation between NCC, TSF, and/or the Trustee.

5.8 Even if Judge Hoyt wanted to ignore the influence of the facts in part IV in order to be neutral and reach an objective decision that is fair and impartial, Judge Hoyt's bias is pervasive and he is not able to do so.

VI.

6.1 This Motion is also brought under the Due Process Clause(s) of the United States Constitution.

6.2 The Due Process Clause(s) of the United States Constitution in the Fifth and Fourteenth Amendments guarantee to TSF the right to trial before an objective, impartial, and fair tribunal and the appearance of an objective, impartial, and fair tribunal.

6.3 If Judge Hoyt is the trial judge or the fact finder, with respect to disputes to which TSF is a

party and in which TSF has an interest that will deprive TSF of due process, in that any such trial will not be a trial before an objective, impartial and fair tribunal for reasons stated above in part IV.

CONCLUSION

VII.

7.1 Judge Hoyt's appearance of bias, if not actual, is so multifaceted and so deep seated as to require recusal.

7.2 TSF is unaware of any attorney who actively participated in TSE's bankruptcy case that believes Judge Hoyt would be a neutral judge and rule in litigation in which TSF is a party objectively, fairly, and impartially.

WHEREFORE, Tri-State Financial prays for an order that Judge Hoyt recuse himself or be disqualified in all litigation of every kind and nature in the Chapter 7 case of TSE in which TSF either is a party or has an interest, including all contested matters and all adversary proceedings.

Dated this 29th day of June, 2006.

TRI-STATE FINANCIAL, LLC

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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF SOUTH DAKOTA
NORTHERN DIVISION

IN RE: TRI-STATE ETHANOL COMPANY, LLC, Debtor.	Case No. BK 03-10194 Chapter 7 **AFFIDAVIT OF GRACE "MIMI" LARSEN** (Filed June 29, 2006)

STATE OF SOUTH DAKOTA)
) ss.
COUNTY OF Roberts)

Affiant Grace ("Mimi") Larsen being first duly sworn, deposes and on oath says:

1. I live in Rosholt, South Dakota.

2. I am an adult over 21 years of age.

3. I am employed as a staff writer for the Rosholt Review, a newspaper in Rosholt, South Dakota. I have been a staff writer for the Rosholt Review for more than seven years.

4. As a staff writer for the Rosholt Review, I have been writing stories about the ethanol plant built by Tri-State Ethanol, LLC ("TSE") located in the northwest corner of South Dakota (the "Ethanol Plant") for over seven years.

5. This Affidavit is based on my firsthand knowledge.

EXHIBIT A

6. Many farmers local to Rosholt, South Dakota, invested money in the Ethanol Plant, some investing money they really didn't have. The progress of the Ethanol Plant, starting with the planning, and continuing with the raising of equity, the construction, the start up difficulties, the explosion, and then through the subsequent bankruptcy case to date, has been of high interest to the local farmers that had invested money in the Ethanol Plant and they have attentively followed the stories I have written about the Ethanol Plant.

7. On October 26, 2004, I attended proceedings in Bankruptcy Court presided over by Judge Hoyt at which the Ethanol Plant and related assets were auctioned off. Before the proceedings began, Judge Hoyt scanned the list of those present that had been compiled by his clerk. I raised my hand when Judge Hoyt asked if there were any not on the list, and I gave him my name and informed him that I was a reporter for the Rosholt Review. He teased me a bit about my name (Mimi), was it my "given" name or not, etc.

8. Three qualified bidders attended the October 26, 2004, proceedings to participate in the bidding. One was ABUS, an organization out of Australia. Another was a California-based company ("EXL"). The third was Tri-State Financial, LLC ("TSF") a number of whose members are based in Omaha. Those Omaha investors in TSF are often called the "Omaha Group." One of the Omaha Group is John Hoich.

9. Before October 26, 2004, I had acquired a list of the "rules" laid out by the Chapter 7 Trustee, John Lovald. I had caused them to be printed in an article in the Rosholt Review on 9-27-04 ("Trustee Files Motion for TEC Sale"). Those rules specified the dates that the sale must close and the date to which the unsuccessful bidders must hold their bids open.

10. Those rules were not followed. Instead, the proceedings bordered on drama and were an exercise in gamesmanship. For the better part of the day, there was wrangling over changing the "rules" and the date by which the successful bidder would be required to close the sale. There was also wrangling over changing the "rules" with respect to how long unsuccessful bidders would be required to keep their bids open past the closing date. (If the successful bidder failed to close, the next bidder would be bound.) In between the wrangling there were recesses. At one time in the proceedings, Judge Hoyt asked me what my headline would be and I replied in exasperation, "Gamesmanship abounds!"

11. There came a time in the afternoon that ABUS said that they (ABUS) would not bid unless the closing date were at least five weeks later than the closing date in the "rules". At one point the attorney for ABUS even stated that they were out of bidding. Judge Hoyt showed extreme preferential treatment toward ABUS, backpedaling from the original closing date to keep them in the bidding. At another time, Judge Hoyt threatened to continue the proceedings and the bidding to another day unless all

participants agreed to changes in the "rules". In my opinion, that bordered on blackmail.

12. In the afternoon, after lunch, and after meeting with ABUS, Robert Hayes, the attorney for John Lovald, the Trustee, told the courtroom that ABUS was willing to make a "non-conforming bid" if the closing date could be changed from early in November to the middle of December. The "non-conforming bid" was eventually disclosed to be $25 million. This disclosure obviously affected Judge Hoyt, and the pressure on the bidders was so great, they had no choice but to agree to the "rules" changes. The closing date was extended by five weeks, EXL dropped out, and only ABUS and TSF remained to bid. TSF agreed to raise the bid of ABUS from $25 million to $25.1 million and bidding between the two followed. These legal gymnastics were astounding. What was the point of pre-approved ground rules if they were altered to the benefit of one bidder?

13. Throughout the bidding, John Hoich sat at counsel table with TSF's counsel, Jerrold Strasheim. Hoich instructed Strasheim what TSF would bid and through Strasheim made all the bids for TSF in a pressure-packed environment. Hoich, near the end of the bidding, looked at David VanderGriend for guidance whether to bid $27.9 million, got a thumbs down, and instructed Strasheim to bid $27.9 anyway. When ABUS bid $28 million, Hoich finally decided not to bid further. Strasheim so informed Judge Hoyt.

14. At one of the recesses, I had asked Judge Hoyt's clerk if I would be able to interview Judge Hoyt after the hearing. The reason I wanted the interview was that I viewed the proceedings as unfairly favoring ABUS, and I wanted to find out why Judge Hoyt was favoring the Australians. Judge Hoyt returned from the recess and said he had a bet with his clerk as to what my name was (whether Mimi or Bebe), which Judge Hoyt won. I was given permission for an interview with Judge Hoyt after the proceedings.

15. After the bidding, and after most of the people had left the courtroom, I interviewed Judge Hoyt in his chambers. No one else was present. Judge Hoyt told me not to take notes. He did not tell me our conversation was off the record. Otherwise, I would not have given this affidavit.

16. In the interview, Judge Hoyt was all grins but I was not happy about the proceedings I had witnessed.

17. At the beginning of the interview, I told Judge Hoyt that the people in Rosholt were unhappy about the outcome. Judge Hoyt was surprised and asked why. He obviously thought the Rosholt people would be glad. I explained to Judge Hoyt that no one in Rosholt wanted the Australians to own the plant. I also explained that ABUS had hired two of the least reputable men in the area to perform "due diligence" for ABUS, and if those two men ran the business, it is doubtful anyone in the area would apply for jobs at

the Ethanol Plant. Judge Hoyt did not know up to that point that Rosholt investors had pooled their money with TSF to enable higher bidding.

18. In the course of the interview, Judge Hoyt brought up John Hoich. Judge Hoyt made no effort to hide his strong dislike for John Hoich. Judge Hoyt volunteered to me that in a previous hearing John Hoich had gotten on the stand, acted arrogant, and, among other things, testified that he (Hoich) was worth millions and could buy the Ethanol Plant himself. Judge Hoyt obviously had a very strong negative reaction to Hoich personally on that occasion, based apparently not only on what Hoich had testified to but also on Hoich's manners and demeanor.

19. Judge Hoyt also brought up that Hoich had "hit on" Judge Hoyt's clerk. He was also very hostile to Hoich because of this and expressed very strongly that Hoich should never have done such a thing. I was taken aback by how openly Judge Hoyt disclosed to me the hostility he had toward John Hoich

20. Also in the interview, Judge Hoyt attributed an improper motive to TSF because TSF had hired Strasheim as TSF's attorney. Judge Hoyt, on his own, brought up Strasheim as a subject. His comments were to the effect that Strasheim was a former bankruptcy judge in Nebraska, and TSF thought that the result of hiring Strasheim would be that Strasheim and Judge Hoyt would be "good old boys" getting together, resulting in favoritism toward TSF. Judge

Hoyt told me that he had shown TSF and Strasheim that that would not work. I believe Judge Hoyt was referring to his decision in late July 2004 to convert TSF's Chapter 11 case to Chapter 7.

21. It was obvious to me that Judge Hoyt has a very strong dislike not only for Hoich, but also for TSF, the Omaha group, and perhaps Strasheim and has a clear bias against them. It was clear to me in the interview that Judge Hoyt had actually enjoyed seeing TSF fail to be the successful bidder, mainly because of Hoich but also because of TSF's Omaha group. Judge Hoyt told me, "I didn't mind seeing Hoich sweat," during the bidding. At no time did Judge Hoyt make any comment that I understood to mean that Judge Hoyt was not antagonistic toward Hoich, TSF, the Omaha Group or that he had made or would make any effort to be fair to any of them. The thought that came to my mind was: "kangaroo court."

22. During the proceedings, including the recesses, I also heard several conversations between other attendees (other than the bidders) at the proceedings whose opinions were consistent with mine about the "kangaroo court" idea. These conversations were to the effect that John Lovald, the Trustee, and his lawyer, Robert Hayes, were under Judge Hoyt's thumb and were "only doing what the judge told them to do." These conversations were carried on by persons not associated with TSF. In my experience, the idea that the Trustee and his attorney are under Judge Hoyt's influence was widely and generally

held, but did not come up in the interview I had with the judge.

23. I agreed to write this affidavit in May 2006 for several reasons.

a. It is clear that Judge Hoyt has a strong dislike for, and a deep bias and prejudice against, John Hoich specifically, the Omaha group in general, TSF, and possibly Strasheim, which is clouding his judgement.

b. His judgements involve monetary awards to claimants that will lessen the amount of money left over to reimburse the local people for their investment in the Ethanol Plant (see 6 above).

c. I, and many others close to the bankruptcy case, were baffled and shocked when Judge Hoyt himself forced TSE from Chapter 11 to Chapter 7 Bankruptcy at the moment TSE thought he would accept their reorganization plan.

d. I am especially concerned about the pending award to NCC, having followed the original bid price, the construction process, and having known of questionable construction practices. I perceive a bias in favor of NCC.

/s/ Grace "Mimi" Larsen
Grace "Mimi" Larsen

Subscribed, sworn to, and acknowledged before me this 12th day of June, 2006.

/s/ Carol D. Swartz
Notary Public

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH DAKOTA
NORTHERN DIVISION

IN RE: TRI-STATE ETHANOL COMPANY, LLC,
TAX ID #46-0449270
BANKR. NO. 03-10194 (CHAPTER 7)

TRI-STATE FINANCIAL, LLC, APPELLANT,

v.

ROBERT E. HAYES, DAVENPORT,
EVANS, et al., APPELLEE.

Case No. 06-1040

BRIEF OF APPELLANT TRI-STATE FINANCIAL, LLC

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(A) PARTIES:

The Appellant in this appeal is Tri-State Financial, LLC ("TSF"). The Appellee is Robert E. Hayes, of Davenport, Evans, Horowitz, & Smith, LLP.

(B) BASIS OF APPELLATE JURISDICTION:

Jurisdiction of the District Court for this appeal is based on 28 U.S.C. §158(a)(1) providing that "The district courts of the United States shall have jurisdiction to hear appeals (1) from final judgments, orders, and decrees . . . " Subject matter jurisdiction exists over interlocutory orders underpinning the final order. *Fleet Nat'l Bank v. H&D Entertainment*, 96 F.3d 532, 537 (1st Cir. 1996); *In re Federal Skywalk Cases*, 680 F.2d 1175, 1180-81 (8th Cir. 1982) *cert denied* 459 U.S. 988; 13A Wright, Miller & Cooper, FEDERAL PRACTICE AND PROCEDURE: Jurisdiction 2d §3553 at pp 655-656.

(C) STATEMENT OF ISSUES AND STANDARDS OF REVIEW:

The issues presented are whether the Bankruptcy Court committed reversible error by (i) denying TSF discovery, an evidentiary hearing, and the opportunity to make a full record on TSF's Motion for Recusal; (ii) denying TSF's Motion for Recusal and ruling on the fee application of Hayes ("Fee Application"), notwithstanding appearance of bias, actual bias, and requirements of due process; and failing to

deny Hayes Fee Application on: (iii) invalidity of Hayes' appointment under 11 U.S.C. §327(a); (iv) lack of a valid appointment because of representing an interest adverse to and in conflict with the Chapter 7 estate; (v) failure of due care by Hayes to fully inform the court whether at or after the time of his appointment, Hayes represented an interest adverse to and in actual conflict with the Chapter 7 estate; (vi) lack of candid and complete disclosure by Hayes that Clapper Corporation was the holder of a claim that as disclosed in Schedule F of the debtor, was a disputed claim; (vii) Hayes' failure to candidly and completely disclose that Clapper's claim in the amount of $195,929.43 was disputed and all circumstances of the dispute; (viii) the Trustee, Hayes, or either or both, had actual or constructive knowledge not only that Hayes represented Clapper, but also that Clapper's claim was disputed and was adverse to and in conflict with the interest of the Chapter 7 estate, (ix) binding judicial admission of the existence of an actual conflict of interest at the time of his appointment; (x) failure of the Trustee, Hayes, or either or both to disclose, that the Trustee and Clapper allegedly waived Hayes' conflict of interest; (xi) the alleged waiver of conflict of interest between Clapper and the Trustee is of no legal effect; (xii) Hayes had the burden of proving that at the time of his appointment and thereafter, Hayes represented no interest adverse to or actually in conflict with the Chapter 7 estate and failed to do so; (xiii) making the clearly erroneous finding that TSF stipulated that the fees described in the Fee Application were for necessary services or

benefited the estate; (xiv) Hayes is not entitled to avoid the §327(a) rule prohibiting conflicts of interest by failing to inform himself as to whether there is an actual conflict of interest of not; and (xv) whether the court's failure to deny the Fee Application of Hayes et al. was an abuse of discretion.

The standards of review for the above are: for due process, a fair trial in a fair tribunal (requires an absence of actual bias) on an adequate record; for recusal (if record adequate), abuse of discretion; for allowance of attorneys' fees, abuse of discretion; for abuse of discretion, whether judgment was based on clearly erroneous factual findings or erroneous legal conclusions; for legal conclusions in general, *de novo*, for findings of fact, clearly erroneous, and for motion to alter or amend, abuse of discretion.

(D) STATEMENT OF THE CASE:

TSF filed a Motion for Recusal praying that, on all or any of several alleged grounds Judge Hoyt should have recused himself or be disqualified in litigation in the Chapter 7 case of TSE in which TSF is either a party or has an interest, including all contested matters and all adversary proceedings. Orders were entered in the Bankruptcy Court that denied TSF the right to discovery on the Motion for Recusal, prevented TSF from having an evidentiary hearing, and prevented development of a full and complete record. Judge Hoyt denied the Motion for

Recusal. The Order denying the Motion for Recusal is an interlocutory order.

On the same day that TSF filed its Motion for Recusal, TSF filed its objections to Hayes' Fee Application. TSF objected to the Fee Application on the grounds that when appointed and thereafter, Hayes had a conflict of interest (undisclosed) and the Fee Application should be denied on that ground. The conflict of interest was that Hayes, while representing the Trustee, also represented the Clapper Corporation ("Clapper") which held a disputed claim which was then $195,929.43.

Hayes filed a response to TSF's objections. Hayes claimed that when appointed, Hayes, by agreement with the Trustee, had obtained a waiver of the conflict of interest from Clapper and the Trustee had waived the conflict of interest.

Although when Hayes was appointed, there was a disclosure that Hayes represented Clapper, there was no disclosure that the claim held by Clapper was adverse to and in actual conflict with the interests of the Chapter 7 estate or of any waiver of conflict of interest.

At the hearing, Hayes testified that when appointed and thereafter until the hearing, he made no effort to inform himself whether there was an actual conflict of interest with the Chapter 7 estate. At the time of Hayes' appointment and at all times thereafter, Schedule F of TSE has shown the claim with

Clapper to be a disputed claim. Judge Hoyt allowed the Fee Application of Hayes.

TSF brings this appeal.

(E) FACTS:

The debtor, Tri-State Ethanol Company, LLC ("TSE") was formed in 1998 to build, own, and operate an ethanol plant in Rosholt, South Dakota ("Ethanol Plant") (#288 at 7). TSE financed the Ethanol Plant with First Dakota National Bank ("FDNB"). North Central Construction, Inc. k/n/a American Prairie Construction Company ("NCC") was the general contractor.

The first ethanol was produced at the Ethanol Plant for sale in May 2002 (#288 at 8). A number of problems were soon discovered with the construction and design of the Ethanol Plant. *Id.* In almost every area of the Ethanol Plant, TSE encountered problems with the Ethanol Plant not functioning as it was intended. From the initial startup of production in May 2002 until December 31, 2002, there were numerous and continuing design/construction problems with the Ethanol Plant's operations (#288 at 9). On at least eight occasions, the Ethanol Plant had to be shut down because of design/construction problems with the boilers; there were numerous power interruptions and outages; and there were problems with the centrifuge (#288 at 8). On December 31, 2002, a spark from an NCC welder caused an explosion at the Ethanol Plant (#288 at 10).

The Ethanol Plant would not and could not function as it was intended – to produce ethanol at its nameplate capacity of 14 MGY. There also were significant cost overruns. NCC filed mechanic's liens for over $3.6 million (#288 at 16). Foreclosures were filed by both NCC and by FDNB (#288 at 12) and by NCC (#288 at 13).

TSE filed a voluntary Chapter 11 case on May 23, 2003 (#1). Between May 23, 2003, and July 29, 2004, TSE was the debtor-in-possession (DIP) in its Chapter 11 case. TSE's Chapter 11 case was converted to a Chapter 7 case on July 29, 2004 (#939). The primary asset of TSE's Chapter 11 and Chapter 7 cases was the Ethanol Plant.

When TSE filed its Chapter 11 case on May 23, 2003, TSE's members included a group of over 20 investors from Omaha, Nebraska, that had invested a total of $2.5 million in TSE (#288 at 14). TSE's board reorganized a complete analysis of the Ethanol Plant was necessary to determine what if any re-engineering and reconstruction (collectively Retrofitting) was needed to start up the Ethanol Plant and have it produce ethanol at a reasonable level (#288 at 18). After TSE filed its Chapter 11, members of the TSE members contacted Dave VanderGriend, a principal in ICM, Inc., a leading firm in the development of ethanol plants throughout the country (#288 at 18). VanderGriend toured the Ethanol Plant in July 2003 and prepared a written report. (*Id.)* The VanderGriend report recommended that each area of the Ethanol Plant be "upgraded to make the plant a

functional facility" and that "if the decision . . . is to partially upgrade, then the recommendation of ICM would be not to start at all." Details of the recommended upgrading were included. (#107, Ex. 1 at Ex. A).

The value of the Ethanol Plant if not upgraded was believed to be insufficient to pay creditors, much less to generate and return to members for equity. (#137, Ex. B at 3; 221 at 21).

Meanwhile, in June 2003, some members of TSE formed Tri-State Financial, LLC ("TSF"), a Nebraska limited liability company (#288 at 17). The purpose of TSF was to collect $2 million to facilitate funding of TSE's Retrofitting of the Ethanol Plant (#288 at 17). Those members transferred their equity security in TSE to TSF in exchange for membership in TSF; and TSF became the equity security holder in TSE in place of the members (#1409).

On September 25, 2003, TSE filed a motion for multifaceted relief (9/24/03 Motion) (#107). The 9/25/03 motion was based on a stipulation entered into by TSE, TSF, and FDNB (9/25/03 Stipulation) attached as Exhibit A. The VanderGriend report was attached to the 9/25/03 Stipulation as Exhibit 1.

By its 9/25/03 Motion, TSE (and FDNB and TSF) sought authorization: to enter into a contract with ICM, Inc. ("ICM") for Retrofitting TSE's Ethanol Plant; to incur debt consisting of loans from TSF and FDNB to pay for the Retrofitting; for such loans to be entitled to super priority over other expenses of

administration and be secured by a post-petition priming first lien on all assets of TSE; for approval of TSE's use of cash collateral in which FDNB had an interest; for TSF and FDNB to have the right of an advance approval of expenditures by TSE for Retrofitting and startup costs; and for the treatment by TSE of FDNB in a then yet-to-be-filed Chapter 11 plan.

After an evidentiary hearing on October 22, 2003 (#222 at 9) at which the witnesses in support of approval of TSF's 9/25/03 Motion, were Vander-Griend, who testified at length (#222 at 9-14), James Jandrain, a certified public accountant (#222 at 14-19), Dan Swanda, a lending officer at FDNB who handled complex loans (#222, at 20-21), and John Hoich, an investor in TSF with a substantial net worth (#222 at 19-20). No witness testified in opposition to TSE's 9/25/03 Motion or in contradiction to the testimony that was given. Attorneys for Gaylor Engineering, the designer of the non-working Ethanol Plant, and of NCC, the builder of the non-working Ethanol Plant appeared at the hearing and opposed the 9/25/03 Motion.

By decision (#222) and order (#223) on December 12, 2003, Judge Hoyt denied TSE's 9/25/03 Motion in all respects ("12/12/03 Decision") and ("12/12/03 Order"). Judge Hoyt's 12/12/03 Decision generally did not credit any of the testimony in support of TSE's 9/25/03 Motion. Judge Hoyt stated that the 9/25/03 Stipulation "was tainted by the fact that Debtor dealt primarily with insiders" (#222 at 28). He also stated

in summary that aspects of the 9/25/03 Stipulation were akin to a plan, that TSE failed to show that the necessary credit and use of cash collateral for the Retrofitting could be obtained only through a super priority lien, discrediting Jandrain's testimony, and there was a failure to show that existing creditors were protected (#222 at 27-29).

Before the 12/12/03 Decision and the 12/12/Order, TSE and ICM, with assistance from TSF had begun to Retrofit the Ethanol Plant. The contractor, ICM, had significant work commencing in early 2004 and was concerned about being able to complete the work at TSE if ICM deferred the starting date. Even though the Retrofitting had begun, there was no contract between TSE and ICM (#288 at 22).[1]

When Judge Hoyt denied TSE's Motion by the 12/12/03 Decision and the 12/12/03 Order, TSE, ICM, and TSF continued to Retrofit the Ethanol Plant. They did so without TSE making any contract with ICM; without any super priority for loans by TSF and FDNB ahead of other administrative expenses, and without any post-petition priming first lien on TSE's assets for any loan. They also did so to protect and preserve TSE's estate, mainly the going concern value of TSE's Ethanol Plant. In the process of Retrofitting,

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[1] By denying TSF an evidentiary hearing on TSF's Motion for Recusal, Judge Hoyt prevented TSF from proving that starting the Retrofitting was on advice of their former Omaha counsel, William Biggs.

ICM increased the name plate capacity of the Ethanol Plant from 14 MGY to 20 MGY.[2]

On December 31, 2003, TSF filed a Disclosure Statement (#241). In that 12/31/03 Disclosure Statement, TSF fully and completely disclosed that VanderGriend and ICM were Retrofitting the Ethanol Plant without any written contract; that VanderGriend understood he may not be paid for the Retrofitting in the event no plan was confirmed or in the event the Ethanol Plant did not operate; that no funds of TSE are being used other than for payment of salaries of existing employees of TSE "who have continued to maintain the premises throughout the proceeding" (#241 at 20). The disclosure statement concluded that TSE "is hopeful that prior to confirmation of the plan, the plant can be restarted which will be a benefit." (#241 at 20).

On January 30, 2004, TSE, TSF, and First Dakota National Bank filed a Stipulation for Chapter 11 Plan Treatment ("1/30/04 Stipulation") (#269). The 1/30/04 Stipulation, conforming to Judge Hoyt's 12/12/03 Decision and 12/12/03 Order as to the 9/25/03 Stipulation being akin to a plan agreed to the treatment of First Dakota National Bank in a Plan of Reorganization (#269) to everyone involved, including

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[2] See note 1 above. Similarly, the denial of an evidentiary hearing on TSF's Motion for Recusal prevented TSF from proving this was also on the advice of former Omaha counsel, William Biggs.

all creditors" (#241 at 20), but would require acceptance and confirmation of a plan as Judge Hoyt had mandated.

On February 17, 2004, TSE filed an Amended Disclosure Statement for Debtor's Plan of Reorganization" (#288) again there was full and complete disclosure with language which is nearly identical to that quoted above for the December 31, 2003, Disclosure Statement (#288 at 22) but with the following additional disclosure:

> "It is the Debtor's intention that approval of the ICM contract for the reengineering and reconstruction will come with confirmation of the Plan, although that approval may be after the fact however. Both ICM and the Debtor desired to move the work forward. ICM has undertaken the reengineering and reconstruction without any guarantee of payment whatsoever. That process should be completed some time in April. A full copy of the signed contract, along with the proposal for reengineering and reconstruction and fee schedule are attached to the Debtor's response to NCC's initial objection to the Disclosure Statement and will be made available to anyone who desires a full copy.
>
> "ICM and VanderGriend are volunteers. They understand that the Court has not sanctioned the ICM contract. The Debtor understands that as well. If the work is completed successfully, and the plant operates

> profitably, ICM will be paid. In addition to VanderGriend and ICM volunteering to proceed with the reengineering and reconstruction, Tri-State Financial has also advanced substantial funds on an unsecured basis for the purchase of equipment. It owns the equipment and is having it installed by ICM as part of the reengineering and reconstruction. If the work is completed successfully and the plant operates profitably, Tri-State Financial will be paid for the equipment." (#288 at 22-23).[3]

On February 25, 2004, Judge Hoyt entered an order approving TSE's February 17, 2004, Amended Disclosure Statement (#299). On March 2, 2004, an amended order was entered again approving TSE's Amended Disclosure Statement (#315).

On December 23, 2003, William L. Biggs of Gross & Welch, an Omaha law firm, a lawyer who represented TSE along with A. Thomas Pokela of Sioux Falls, SD, filed an interim fee (and expense) application for $90,492.63 (#237). On January 27, 2004, Judge Hoyt wrote and filed a letter to Biggs. The letter included that "if the objections [by United

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[3] Compare Judge Hoyt's statement on page 23 of his Decision denying TSF's Motion for Recusal that an objection filed by Tri-State Corn Processors on June 8, 2004, "was the first indicating the court found in the record that re-engineering work [defined in note 3 on p7 to include reconstruction] had continued, even though Debtor [TSE] had failed to obtain court approval for that work."

States Trustee and NCC] are correct that William L. Biggs or other members of Gross & Welch have been rendering services in case for other than Debtor, Gross & Welch's entire fee application may be for naught . . . and the order approving the firm's employment as counsel may need to be vacated," citing two rulings of his own. (*Id.*) He added that he would leave it to the assistant United States Trustee and the attorney for NCC "to conduct whatever further investigation they may want to do on Gross & Welch's pre- or post-petition conflicts of interest and, if appropriate, file a motion to vacate the firm's employment order." (*Id.*) The reference to conflict of interest in Judge Hoyt's letter was that Biggs represented both TSE and TSF (#263). On February 27, 2003, Judge Hoyt approved the withdrawal of Biggs and Gross & Welch fee application as moot, and dismissed the United States Trustee's Motion to vacate the order approving the employment of Gross & Welch as attorney for TSE as moot (#308). Thereafter, on March 8, 2004, Biggs filed a written appearance in the case for TSF but was not heard from again in TSE's case.

Shortly before June 21, 2004, TSF engaged Jerrold L. Strasheim, Omaha, Nebraska, as the new counsel in the Chapter 11 case of TSE. In a hearing on June 21, 2004, Ron Hall, attorney for NCC with Strasheim's consent recited that they had reported an agreement which was recited in the hearing. The terms of the recited agreement were that TSF would pay NCC, and its subcontractor, Interstate Electric &

Engineering Co. ("IEEC"), $2,500,000, of which $1,500,000 was to be allocated to NCC's and IEEC's claims and $1,000,000 would be allocated to equity; and TSE would file an amended plan under which TSF as successor to NCC and IEEC would have an allowed secured claim of $1,500,000; and objections of NCC and IEEC to confirmation would be withdrawn. The parties agreed that a written agreement would be prepared. Later it developed that TSF collected the $2,500,000 to be ready to perform but NCC would not agree that a condition was that TSE's plan would be confirmed and no written agreement was ever achieved.[4]

Absent the written agreement, NCC decided to claim the June 26, 2004, recitation in and of itself was enough. NCC moved to enforce the "Agreement" before Judge Hoyt (#836). NCC claimed what had been recited in court on June 21, 2004, was binding. This was that TSF and NCC would enter into a $2.5 million written settlement agreement, $1.5 million for NCC's claim which would be paid by TSE under a

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[4] NCC's initial draft of the written agreement would have made confirmation of TSE's plan automatic approval of the written agreement; it would have assigned claims described as being in classes (there are classes in Chapter 11 but not in Chapter 7); it also made the parties to the agreement include John Hoich as a party and he was not at the hearing or represented at the hearing; and it would have made First Dakota National Bank a party. Several drafts were exchanged. Judge Hoyt has been provided with the evidence of that but in denying TSF's Motion for Recusal said he had not looked at it (#1917 at p. 63, n. 8).

plan and $1 million for equity. On July 27, 2004, there had been a meeting in Judge Hoyt's chambers followed by a meeting on the record. On the record, Judge Hoyt said that absent that agreement between TSF and NCC (and payment by TSF of $2.5 million):

> "THE COURT: Well let me put it this way. We just had a short discussion on confirmation and if this matter is, is left unresolved, it would appear to me based upon my unlimited knowledge,[5] that confirmation may be difficult to obtain. And as I'd indicated earlier, if confirmation isn't obtained then I am going to act on – I think it's the United States Trustee's motion to dismiss." (Tr. 7:27/04 hearing at 4:17-23).

On the record, Judge Hoyt on July 27, 2004, ruled "Parties could not finalize the Agreement. The motion was rendered moot." (#933).

The next day, July 28, 2004, was the scheduled day to consider the confirmation of an amended plan that TSE had filed on June 25, 2004 (#1366), and a motion that the United States Trustee had filed to dismiss or convert the case to Chapter 11. TSE joined in the United States Trustee's motion to dismiss. Judge Hoyt took up whether to dismiss or convert. Although not directly germane to the issues to be decided, Judge Hoyt denounced those associated with

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[5] Judge Hoyt had no evidence of the drafts and correspondence exchanged after June 21, 2004, in an effort to arrive at a written agreement. *See also* note 4 above..

Retrofitting of the Ethanol Plant as having disregarded his judicial authority, abused the bankruptcy process, and put into action a nefarious scheme to get control of TSE:

> " . . . what the approach has been in this case [is] it's better to get forgiveness than permission, cause all of these things, as you well know required permission. And when permission was refused initially, then they just went off and did it and said we'll see if we can get forgiveness when it comes time for confirmation. . . . " (Transcript[6] 7/28/04 hearing at 72:10-15).
>
> "So what we, what we engaged in is we engaged in a plan to significantly expand the plan and eventually, the way this was structured, there would be a new equity group created and the old equity group would go away. That's what was going to happen if, if there had been a confirmation." (*Id.* at 76:12-16).
>
> "Some? A lot. And that meant the contributions that have been given before, whereas it's going to be lost in the, in the, in the shuffle, number one. There would be a different group of control, number two. And it was an entirely different game, wasn't it?" (*Id.* at 76:19-23)

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[6] Transcript abbreviated hereafter as "Tr."

"Well, I'm, I'm – what I'm saying is that the plant was at – was apparently able to operate as it was originally intended, whether that was an inefficient or efficient we don't know for sure. . . . "[7] (*Id.* at 77:1-4).

" – prior that it was an inefficient operation and needed to be brought up to seventeen to eighteen to twenty million gallons and, everything would be great. I had never heard before today that we were on the doorstep of having this thing ready to go. And what really has taken place here was the, the use of the bankruptcy process to infuse money into this and in essence – and, and it was – and in what – what in essence was going to happen was going to be a change of control, and I'm picking on the wrong person. I shoot my arrow in the wrong direction." (*Id.* at 77:6-15).

" . . . from what I've seen it would be very hard to call this a good faith filing . . . " (*Id.* at 89:17-18).

Judge Hoyt did not acknowledge the disclosure by TSE of the ongoing Retrofitting in TSE's 12/31/03 Disclosure Statement and in TSE's 2/17/04 Amended Disclosure Statement, which he had approved, of that the ongoing Retrofitting of the Ethanol Plant was on a voluntary basis without contract or the disclosure to

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[7] It is unknown what substantive evidence exists to support that the Ethanol Plant was able to operate as it was originally intended. TSF dispute there is such evidence.

the United States Trustee in TSE's reports that TSF was loaning TSE money for insurance, payroll of some employees, and other TSE expenses of maintaining the Ethanol Plant; that after 12/12/03 he never ordered TSE to stop Retrofitting the Ethanol Plant; nor did Judge Hoyt acknowledge there was on file a Modified Plan of Reorganization that TSE had filed on June 25, 2004 (#701), which with respect to equity in summary provided that: holders of equity security in TSE would retain their equity securities that they held on May 23, 2003, when TSE filed Chapter 11; new investments of approximately $3.5 million would be required to pay for the initial Retrofitting and the startup of the Ethanol Plant; that all holders of equity securities on May 23, 2003, had the right to make new investments toward the $3.5 million in amounts necessary for such holders to keep the same percentage of ownership in TSE as they held before May 23, 2003.[8]

In addition to denouncing TSE, TSF, and ICM, Judge Hoyt announced that he would not have confirmed the Chapter 11 Plan of TSE.[9] After TSE withdrew its request for confirmation of the June 25,

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[8] In fact, by conversion to Chapter 7, all equity holders lost all their equity. Under the Chapter 11 plan, as indicated above, all original equity holders would have retained their equity interest and were offered the right to contribute additional equity to avoid dilution.

[9] Judge Hoyt's comments quoted above about equity suggest that the [sic] may have been talking about other than TSE's Plan filed June 25, 2004 (#701).

2004, Plan (#701), Judge Hoyt disclosed that because of his independent duty to apply confirmation standards, whether there were objections to confirmation or not, he probably would not have confirmed TSF's Chapter 11 plan, mainly because of lack of feasibility and lack of good faith. (Tr. 7/28/04 hearing at 88:21-89:18). A reasonable inference is that a fair judge would have mentioned the noncomfirmability or at least the uncertainty of confirmability of TSE's Plan on July 27, 2004, when the issue was whether TSF was obligated to pay $2.5 million to NCC in a case that Judge Hoyt was nearly certain would be converted a Chapter 7 case. TSF could have unknowingly been agreeing on July 27, 2004, to pay $1 million for equity in a Chapter 7 case and $1.5 million for a claim which would not be paid under a confirmed Chapter 11 plan and in a Chapter 7 case would be a hotly disputed claim.

Judge Hoyt also found requirements for conversion were met; and announced his decision to convert TSE's Chapter 11 case to Chapter 7 (*Id.* at 89:14-92:11). The next day, on July 29, 2004, Judge Hoyt entered an order of conversion (#939).[10]

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[10] Had there been an evidentiary hearing on TSF's Motion for Recusal, TSF would have had the opportunity to present evidence of how the day before Judge Hoyt announced his independent duty to see that requirements were met. Judge Hoyt, in chambers, was attempting to influence TSF to pay $2.5 million to NCC without the condition that TSE's plan could be confirmed.

When TSE's Chapter 11 case was converted to Chapter 7 on July 27, 2004, John S. Lovald, the appointed Chapter 7 Trustee, recognized that the Ethanol Plant was of much greater value if the Retrofitting of the Ethanol Plant were completed and the Ethanol Plant began operating. Lovald sought to engage VanderGriend and ICM to continue the Retrofitting. On August 3, 2004, Lovald filed a Motion for Authorization to Operate the Business, to Incur Secured Debt, and Used Cash Collateral (#946). Lovald's 8/3/04 Motion stated in paragraph 5 that the Ethanol Plant "as originally constructed was subject to numerous design and construction defects," and in paragraph 8 that VanderGriend of ICM stated that he "was prepared, upon court authorization to complete the construction . . . ". The Trustee sought to prime other liens to pay for the cost, and had attached a budget projecting the need for a $1,500,000 Construction Loan plus a $2,500,000 Start-up and Operating Loan, or a total of $4,000,000. The Trustee declared the source of the $4,000,000 was individuals associated with TSF or TSE (#954). Judge Hoyt deferred and never authorized the primary loan (#988) on request of Lovald, the Trustee.

On August 3, 2004, Lovald filed an Application for Approval of Employment of Attorneys in which he asked to employ Robert E. Hayes (and Keith A. Gauer) of Davenport, Evans, Hurwitz & Smith, LLP (all hereafter and hereinbefore collectively "Hayes") generally as attorneys for the Trustee in TSE's Chapter 11 case (#948). Lovald's 8/3/04 application recited

that Hayes had disclosed that "Hayes is counsel for unsecured creditor Clapper Corporation." There was no other disclosure of any kind. Attached to Lovald's 8/3/04 was a "Verification" by which Hayes declared "under penalty of perjury that the foregoing is true and correct according to the best of their knowledge, information and belief." There was no disclosure by Lovald or Hayes of any "waiver of any conflict of interest" by Clapper Corporation ("Clapper") and the Trustee. On August 11, 2004, Lovald's 8/3/04 Application was approved (#962). Schedule F of TSE, which was not mentioned, however, filed on June 6, 2003, showed that Clapper's claim was disputed. Thereafter, Hayes performed a wide range of services including representing Lovald in the sale and disposition of the assets of TSE and in opposing some claims and paying some claims. (894, 994, 1007, 1008, 1009, 1024, 1025, *Id.* 1124, 1144, 1146, 1147, 1148, 1150, 1151, 1165, 1185, 1190, 1211, 1226, 1237, 1250, 1251, 1258, 1267, 1274, 1275, 1372, 1373, 1379, 1424 designated Ex. TSF-4 through TSF-34).

On September 10, 2004, Lovald, through Hayes, filed a Motion for Establishment of Bidding Procedures For Sale of All or Substantially All Assets of the Debtor through Hayes, mainly, of course, the Ethanol Plant (#944). On September 22, 2004, Judge Hoyt entered an Order granting Lovald's 9/10/04 Motion. Lovald's 9/10/04 Motion and the Court's 9/22/04 Order, among other things, provided for an auction on October 22, 2004, conducted by Judge Hoyt. They also required bidders to meet stated standards to become

"Qualified Bidders." Among other things, Any Qualified Bidder was required to demonstrate the capacity to close on or before November 1, 2004, nine days after the October 22, 2004, auction. Judge Hoyt's 9/22/04 Order directed Lovald to move for a sale of substantially all of the assets of TSE's Chapter 7 estate free and clear of all liens and all interests. Also, on September 22, 2004, Lovald submitted a motion for sale as directed (#1009).

Lovald's September 22, 2004, Motion in paragraph 2 said that $20,300,000 was a fair and reasonable value. That $20,300,000, according to paragraph 3, was to be comprised of $18,000,000 cash plus assumption of certain obligations owed for the post conversion completion "estimate" of $1,500,000. Lovald's Motion recited that, as Trustee, Lovald already had received an initial bid for $20,300,000 from EXL Group, LLC, and provided that if there were other timely "Qualified Bids" according to standard set out in the Motion which tracked those in his earlier August 3, 2004 Motion for Authorization to Operate the Business, there would be an auction by Judge Hoyt on October 22, 2004. It required that the successful bidder demonstrate the ability to close on or before November 1, 2004.

On October 4, 2004, TSF filed a Motion to Clarify, Amend, or Reconsider the Bidding Procedures Order (#1014). Among other things, TSF in paragraph 10(b) asked that the date by which Qualified Bidders must demonstrate ability to close be changed from November 1, 1004 [sic], on condition that the successful

bidder assumes the expenses of maintaining the Ethanol Plant from November 1, 2004, to December 1, 2004. TSF alleged that expenses to obtain financing for TSF's Qualified Bid amounted to $300,000 or more; to close a sale of the Ethanol Plant for over $20,000,000 in nine days is not commercially reasonable; and lenders ordinarily require 30 days to provide the funding.

On October 8, 2004, the Court denied TSF's Motion requesting a December 1, 2004, closing date (#1025). Later the auction ended up being held on October 26, 2004, rather than October 22, 2004, and the November 1, 2004, closing date automatically got changed to November 4, 2004.

TSF had the ability to close by November 4, 2004 (Tr. 10/26/04 hearing at 42:15-18). However, ABUS, another "Qualified Bidder,"[11] even though it refused to bid if the closing were November 4, 2004, was permitted to make a "nonconforming" bid with a closing date of December 15, 2004 (*Id.* at 48:15-49:1). The Court suggested to Hayes that if TSF – then the only bidder against ABUS – would not agree to a December 15, 2004, closing date, Lovald should withdraw his motion for sale and file a new motion (*Id.* at 49:2-12). Lovald, through Hayes, then used the threat of withdrawing his motion for sale rather than continue with the bidding in order to obtain TSF's agreement

[11] ABUS, although accepted by Lovald as a qualified bidder, turned out to be unable to close by December 15, 2004.

to an extension of the closing date to December 15, 2004, even though the Court had refused TSF's written motion for extension of the closing date to December 1, 2004. (*Id.* at 52:2-19). TSF had to also agree to keep its bid open to December 22, 2004 (54:3-8).[12]

The nonconforming bid of ABUS turned out to be in the amount of $25,000,000. (*Id.* at 54:14-19). ABUS was supposed to have demonstrated to Lovald on November 4, 2004, the ability to close on December 15, 2004 (*Id.* at 68:9-16) but it is doubtful ABUS ever did. ABUS ended up the highest bidder but failed to close on December 15, 2004. TSF was the next highest bidder #1121) and ended up with TSE's assets but for a higher price ($27,900,000) than should have been the case. (*Id.* at 68:17-19) (TSF-24; #1237).

Grace (Mimi) Larsen ("Larsen") was in attendance at the October 26, 2004, auction conducted by Judge Hoyt. She was employed by the *Rosholt Review*, a newspaper in Rosholt, South Dakota, as a staff writer, and had had been writing stories about the Ethanol Plant for over seven years. She had printed the bidding procedures in the *Rosholt Review*. As expressed in her June 12, 2004, affidavit (#1873, ex. A), the October 26, 2004, proceedings were preferential towards ABUS; and she was of the impression

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[12] The terms of the sale included that if the successful bidder failed to close, that bidder lost its down payment and the second place bidder was obligated to buy for a stated period.

that Judge Hoyt's suggestion to Hayes to continue the proceedings to another day "bordered on blackmail". She had the thought it was a "kangaroo court". She heard conversations between other than the bidder during recesses that were consistent with the "kangaroo court" idea. Their conversations were to the effect that Lovald and Hayes were under the thumb of Judge Hoyt, and they were only doing what Judge Hoyt told them to do. She said this idea was widely and generally held. As discussed more below, Larsen had an interview with Judge Hoyt after the proceedings on 10/26/04 in which he expressed hostility and bias against John Hoich and possibly also Strasheim, TSF's attorney.

As shown by the Larsen Affidavit, Judge Hoyt strongly dislikes and is antagonistic toward John Hoich, a member of TSF, possibly because: in Hoich's testimony as a witness in support of TSE's 9/25/03 Motion on October 22, 2003, Hoich testified that he had a net worth of $25 million to $30 million (#222 at 20) and had the ability by himself to pay to Retrofit the Ethanol Plant; Hoich was instrumental in causing Dave VanderGriend to become involved with TSE and causing ICM to Retrofit the Ethanol Plant during TSE's Chapter 11 case, expanding its nameplate capacity from 14 MGY to 20 MGY; Judge Hoyt heard in testimony on July 28, 2004, that Hoich with ICM was funding the Retrofitting (Tr. 7/28/04 hearing at 11:19-21); or because, as shown by the Larsen Affidavit, Judge Hoyt believes that Hoich "hit on" Judge Hoyt's law clerk. Also, Judge Hoyt experienced and

expressed pleasure in seeing Hoich "sweat" in the public auction of the Ethanol Plant on October 26, 2004, during which TSF lost out in its attempt to buy the Ethanol Plant from Lovald, the Trustee.

Judge Hoyt knows from Jandrain's testimony in support of TSE's 9/25/03 Motion on October 22, 2003 (#222) that Jandrain is a member of TSF. Judge Hoyt also knows from that testimony, or that of John Hoich, or that of Dave VanderGriend, that Jandrain was instrumental in causing VanderGriend to become involved with TSE and Retrofit the Ethanol Plant, increasing its capacity from 14 MGY to 20 MGY in the process. (*Id.*)

Judge Hoyt has implicitly, if not explicitly, accused important witnesses associated with TSF of not being truthful. In the hearing held on October 22, 2003, on TSE's 9/25/03 Motion to approve the 9/25/03 Stipulation and Agreement between TSE, TSF, and FDNB, Judge Hoyt, without evidence to the contrary, chose to disbelieve the testimony of Hoich, Jandrain, and Randy Kramer, the reasonable testimony of Dave VanderGriend, who then had successfully retrofitted 15 ethanol plants, and the testimony of Daniel Swanda, loan officer of FDNB, to whom TSE owed more than $9 million, approximately half of TSE's total debt (#222). With respect to two members of TSF, James Jandrain and Randy Kramer, Judge Hoyt also impugned their motives. He decided that the 9/25/03 Stipulation and Agreement was "tainted" because it involved Jandrain and other insiders and provided a "hold" on litigation brought by FDNB on

personal guarantees by Jandrain and Randy Kramer of a $600,000 operating note to FDNB from TSE (#222 at 28).

As shown by the Larsen Affidavit, when TSF retained the services of Jerrold L. Strasheim, who formerly was a referee in bankruptcy and bankruptcy judge in Nebraska, Judge Hoyt without any basis concluded that the motivation of TSF was to improperly influence Judge Hoyt in that Judge Hoyt and Strasheim would have a "good old boy" relationship. Judge Hoyt decided to show Strasheim that would not work, possibly by converting TSE's Chapter 11 case to Chapter 7.

The decision of Judge Hoyt on July 28, 2004, to convert TSE's Chapter 11 case to Chapter 7 (Tr. 7/28/04 hearing at 92:4-5), penalized TSE and TSF for what, according to his own language, Judge Hoyt had decided was the disregard of his judicial authority, but also perhaps for what he had decided was a scheme and also perhaps, as suggested by the Larsen affidavit, to put or keep Strasheim in his place.

Later, Judge Hoyt penalized ICM for the Retrofitting of the Ethanol Plant. (TSF 11; ##1120; 1131; 1137; 1159; Tr. 5/4/06 hearing at 18:6-19:8). When ICM filed an Application for Administrative Expenses in TSE's Chapter 11 case for $2,310,552.51 (#1115) for the Retrofitting, including an allegation that the Retrofitting was done in the ordinary course of business, Judge Hoyt, on October 26, 2004, *sua sponte* wrote a letter to ICM's attorney "to be sure there is no

confusion" and "no judicial determination regarding that important issue [ordinary course of business] has been made" and "ICM has made a significant presumption in that regard." Judge Hoyt also stated that payments of $1,190,000 that ICM had received "may be subject to further scrutiny and possible avoidance and recovery for the estate." (TSF-11; #1120).

Taking his cue from Judge Hoyt's October 26, 2004, letter, Lovald, on November 5, 2004, responded to ICM's Application for Allowance of Administrative Expense, saying among other things, that "an evidentiary hearing should be held to review the facts and circumstances causing ICM to proceed with construction retrofit activities without first obtaining court authority." (#1131). After ICM filed an Amended Application (#1137), Lovald again responded repeating the language in ICM's initial application that is quoted above (#1159). ICM buckled under and agreed that its $2,310,552.51 Chapter 11 priority claim should be allowed as a general unsecured claim (Tr. 5/4/06 hearing at 18:23-19:16). This is so even though the Retrofitted Ethanol Plant sold for $27,900,000; and no one has ever provided any evidence contradicting VanderGriend's claim that the Retrofitting doubled the value of the Ethanol Plant. (#1137, Ex. A at 3).[13]

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[13] The Trustee promptly paid secured and certain priority claims totaling over $16 million in full (#1410).

Judge Hoyt also penalized TSF for TSE's involvement by comments putting TSF's right to payment of Chapter 11 administrative expenses at risk.[14] On January 24, 2004, TSF had filed Request Of Tri-State Financial LLC For Allowance Of Administrative Expenses ("TSF's Request") in the amount of $1,983,654 and a contingent, duplicating proof of claim for the same amount. (##1204, 1274).

Lovald, through Hayes, had initially objected to TSF's Request on February 10, 2005, on grounds implicitly suggested by Judge Hoyt in his October 26, 2004, letter on ICM's Application, alleging the "funds advanced [by TSF] were for purposes not authorized by the court, nor for activities performed in the ordinary course of business, and the claims should not be approved as an administrative claim." Lovald had further objected that TSF's Request should not be allowed "as an unsecured claim but should be given a priority status subordinate to unsecured claims, but with a priority as to equity." (#1239). TSF's Request was for reimbursement of TSE's day-to-day expenses

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[14] Lovald piled on by objecting to claims of members of TSF, mainly Jandrain and Kramer, on grounds which he did not assert to object to any other claims including the claims of Woods, Fuller, Schultz & Smith and NCC (## 261, 395, 349). Other than the administrative/clerical process of deleting duplicate claims and sorting out equity/creditor claims, to the best of TSF's knowledge, Lovald elected to dispute or challenge of claims of TSF members on his own volition: Jandrain, Kramer, ICM, and the farmers. Out of approximately 300 claims, the odds of disputing only the four TSF members' claims are approximately 1 in 330,000.

of maintaining the Ethanol Plant during the time TSE was a DIP in Chapter 11 and for equipment. The advances by TSF to TSE for day-to-day expenses were for such items as payroll to TSE employees, insurance, and were in the amount of $793,654.52. The advances for equipment were in the amount of $1,190,000. The equipment was installed by ICM in the Ethanol Plant as part of the pre-conversion Retrofitting (#1204, Ex. A).

Although not associated with the Retrofitting of TSE's Ethanol Plant, Randy Kramer is a member of TSF. Judge Hoyt appears to have penalized Kramer and Jandrain for being members of TSF (##1489, 1554, 1664, 1803, 1914). The issue here is not as to the rulings but as to singling out Kramer and Jandrain and not applying the same rules and disallowing the claims of others such as NCC or Woods, Fuller, Schultz, and Smith, P.C. on the same grounds.

Judge Hoyt scheduled a March 2, 2005, telephonic hearing on Lovald's objection to TSF's Request for argument on whether the Trustee's Objections to TSF's Request should be sustained without an evidentiary hearing. Implicit in that action by Judge Hoyt was his unfair predisposition that his 12/12/03 Decision and 12/12/03 Order barred TSF from any relief. No evidence was offered in that telephonic hearing. Afterwards, on March 14, 2005, Judge Hoyt issued a letter listing items that no one had offered in evidence (#1267). The letter, in relevant part, included a list of occasions (for the benefit of the Trustee) on which TSE got court authorization for

transactions, the implication being the absence of court authorization should be dispositive.[15] The letter also included a list (for the benefit of the Trustee) of some contents of the 9/25/03 Motion that had been denied and of the 9/25/03 Stipulation. And the letter included a summary of Judge Hoyt's 10/26/04 letter concerning ICM's claim. Judge Hoyt also summarized TSF's Request and Proofs of Claim (one for advances and one for equity); and summarized Lovald's objections to TSF's Request. In addition, Judge Hoyt provided a proposed review of law (for the Trustee's benefit) of ordinary course of business – which was flawed or at least incomplete. He did not mention all bases later briefed by TSF for allowing TSF's Request (#1366).

In the same March 2, 2005, telephonic hearing, TSF argued that since the Trustee in his Objection was not only objecting but also seeking to equitably subordinate to other allowed claims any claim of TSF's that was allowed, the Trustee was obligated by the plain language of Fed.R.Bankr.P. 7001(8) to file an adversary proceeding, not merely an objection. Judge Hoyt announced that he would require the Trustee to file a complaint starting an adversary proceeding. The Trustee filed the complaint on March 14, 2005 (#1275; TSF-30). He not only asked

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[15] When the court denied TSF an evidentiary hearing on TSF's Motion for Recusal, it prevented TSF from proving that when cash collateral of FDNB was involved a court order was obtained, but otherwise not.

to equitably subordinate but to recharacterize TSF's debt as equity. Then without warning or request, on March 23, 2005, Judge Hoyt *sua sponte* entered an order shortening the time for TSF to file its answer to April 8, 2005, fixing April 22, 2005, as the deadline to complete discovery and scheduling a trial on May 2, 2005, thereby arbitrarily depriving TSF of the benefits of the Federal Rules of Bankruptcy Procedure for adversary proceedings (#1295). Later he denied TSF's request for a continuance.[16]

Judge Hoyt refused to grant TSF a reasonable time to prepare for trial (## 1295; 1303). Before the evidentiary hearing on TSF's Request was to start, Lovald and TSF agreed to a settlement. Under the terms of the settlement, TSF agreed that the $1,190,000, which TSF advanced for equipment be allowed as a general unsecured claim rather than a Chapter 11 Administrative Claim and subordinated to other allowed general unsecured claims. (Tr. 5/4/06 hearing at 10:4-12:9)

Judge Hoyt later stated that TSF has done wrong in a hearing held on November 18, 2005, in discussing whether the Trustee, NCC, and TFS had made an enforceable agreement, the following:

> "We have every indication here that everybody had supposedly agreed to this and now all of a sudden it's coming apart and

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[16] Later, the trial was moved to start on May 12, 2006, because of a death in Strasheim's law firm.

Tri-State Financial, if, if everybody is, is on the same page, appears to be now trying to change or undermine the earlier settlement that was made in front of Judge Simko." (Tr. 11/18/05 hearing at 10:7-11).

. . .

MR. STRASHEIM: "And I have these comments, Your Honor. I, I would say to begin with, until the Court has seen the drafts and the e-mails that were exchanged I strenuously object to the Court announcing that it's Tri-State Financial that's the problem here.

THE COURT: "Well, Jerry, everybody's pointing at you, I don't know what that means.[17]

MR. STRASHEIM: "Well – they can only point at us legitimately with evidence.

THE COURT: "Okay. (*Id.* at 10:25-11:9).

. . .

MR. STRASHEIM: "Your Honor, it seems to me, Your Honor, that you're expressing an opinion before the case is before you. I say that respectfully.

THE COURT: "Jerry, the only thing I'm doing is I have listened to everybody here

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[17] Only NCC was pointing at TSF.

that has said, now the deal is changing and you're hung up over ten or twelve words and, and you are the one that's been hanging them up. And, and it may be – it certainly may be, that I'm not pre-judging you, it certainly may be that you're looking out in the – looking out for the best interest of your client but this is the second time that this has happened. The first time it happened was when the, the original deal cratered because you said there was an assumption or it was, it was understood that it would require confirmation before there was the validity to your agreement with North Central to start with which was never on the record.

MR. STRASHEIM: "But you didn't see the, the, the written agreement or the e-mail that we got from Mr. O-Halloran after that.

THE COURT: "Well I know what was said in court.

MR. STRASHEIM: "Well you – and, so did Mr. O'Halloran when he sent me the documents." (*Id.* at 11:19-12:21).

Circumstantial evidence that Judge Hoyt directly or indirectly lets Lovald know what Judge Hoyt wants, and Lovald does what Judge Hoyt wants rather than act independently includes the following: the conversations of neutral attendees that Larsen overheard in recesses on October 26, 2004, as Larsen's affidavit states, these conversations were to the effect that Lovald and Hayes were only doing what Judge Hoyt told them to do. (Larsen Affidavit at ¶6).

The letters characterized as "letter decisions" that Judge Hoyt writes and files that are often roadmaps to the Trustee. These include Judge Hoyt's October 26, 2004, letter relating to ICM and Judge Hoyt's March 25, 2005, letter relating to TSF's Request. The unexplained events associated with NCC's Motion to Enforce Mediated Settlement (#1624). Lovald's response to that motion, through Taylor, said plainly, and over and over, that there was no settlement agreement to enforce (#1639). Law was cited. Then at the hearing on February 9, 2006, Lovald and Taylor, sitting quietly, offered no argument on evidence in support of Lovald's Response that there was no contract. Then when the Court said its decision was that there was an enforceable contract, the following transpired:

> THE COURT: "Okay. So the only thing left now is for the trustee to submit the matter for approval for the Court. I'm not going to order that, that's –
>
> MR. STRASHEIM: "You're not ordering that, Your Honor.
>
> THE COURT: "I'm not ordering that. I've, I've simply ordered there's an enforceable contract that was made on July 28th and they can submit it for approval as an agreement.
>
> MR. LOVALD: "Just so the records clear, we're prepared to proceed, Your Honor.
>
> THE COURT: "Okay.

MR. LEE-O'HOLLORAN: "At – on what time frame?

MR. LOVALD: "I'm going to at least ask my attorney to request accelerated notice, perhaps two weeks because I think everybody's prepared to deal with the same issues.

MR. LEE-O'HALLORAN: "I, I was just going to point that that would be appropriate because I believe that all the parties who might have – a standing to object have already been aware of the court terms since at least November 21 when filed the initial motion pleadings.

MR. STRASHEIM: "I take it, if, if I might and, and I'll address this to the Court, but my understanding when Mr. Lovald says he's prepared to – proceed he doesn't mean in today's case, he means with respect to filing a –

MR LOVALD: "With a motion.

MR. STRASHEIM: – "for filing a motion, even though the Court has not ordered."

(2/9/06 Tr. hearing at 49:20-50:20). Then contrary to everything in Lovald's Response, Lovald, through Taylor, filed Trustee's Amended Motion to Approve Agreement with North Central Construction and Tri-State Financial LLC (#1699) attempting to obtain approval of a compromise on notice under Fed.R.Bankr.P. 9019.

In the May 4, 2006, hearing on Trustee's Amended Motion to Approve Settlement Agreement with North Central Construction and Tri-State Financial, Judge Hoyt denied Lovald's Amended Motion, but promised after retirement to go on "recall status" to deal mainly with TSF, and resurrected the bias against TSF:

> "And I also think probably the trustee is aware, as the other parties are, that I had some concern in reference to that claim by virtue of the fact of how it arose and for lack of a better term, it may be a trite term, the concern for the integrity of the bankruptcy system. So there's your hurdle and I don't if you can get over them." (Tr. 5/4/06 hearing Tr. at 63:16-21).
>
> "And you know what? I'm retiring in August but you're going to love this: I'm going to go on re-call status to finish this case. I'm going to keep this case and finish it because I think it would be unfair to give it to the new judge to get into the middle of the picture. Hell, part of the time, I feel like I've come in in the middle." (*Id.* at 68:2-7).
>
> "I'm serious. I'm going to keep this case. I'm going to finish this case. I don't care if we litigate it for eight months." (*Id.* at 69:16-18).
>
> "And probably, one of the ones – I mean, the one that probably concerns me the most is I cannot find any, in my mind, rational reason for the trustee giving up [to TSF] the potential claim against Gaylor Engineering,

> particularly in light of his testimony that there seems to be a history by virtue of – as they were referred to – "sister cases" which they – sister companies, which they really aren't – a history of exposure of Gaylor in those plants which were the same design, as I understand it, at this plant. So at this point I have not seen any justification for sweetening the pie. And I understand that the testimony is that it was late in the day and "we were trying to get a consensus and this was the last thing that we threw in to get a consensus." I don't think that would qualify to reach the standard of reasonableness of the settlement, particularly in lieu of the fact that there is going to be a shortfall in the unsecured creditors which is now created by virtue of the treatment, for sure, of the $1,190,000 claim which had been moved from the category of a subordinated – subordinated unsecured claim to a general unsecured claim." (*Id.* at 62:22-63:15).

Events before the May 4, 2006, hearing are relevant. Judge Hoyt has disqualifying involvement in settlement. Before November 18, 2005, NCC had, without permission of TSF, sent a letter to Judge Hoyt arguing the parties had reached an agreement in mediation which TSF should be forced to honor, and enclosed forty pages of materials. (Tr. 11/18/06 hearing at 5:1-13). One enclosure was a copy of a partial transcript of mediation proceedings including privileged parts. (*Id.*) Also included was a copy of what NCC claimed was the last draft exchanged

between parties of their settlement efforts to reduce what had transpired in mediation to writing. (*Id.*) Judge Hoyt read the letter and its enclosures. (Tr. 2/9/06 hearing at 22:16-23:18). There was no criticism by Judge Hoyt of legal counsel for NCC for presenting privileged material to Judge Hoyt when they knew, or should have known, not to do so.

In a telephonic conference on November 18, 2005, Judge Hoyt, without the benefit of evidence, again blamed TSF for not agreeing to pay $2,500,000 to NCC on July 28, 2004. Judge Hoyt had no concern that TSF would have paid $1 million for equity in TSE's Chapter 7 case and $1.5 million for a hotly disputed claim in a Chapter 7 case.

Then, as indicated above, in the hearing on May 4, 2006, Judge Hoyt heard and volunteered his strong and critical opinion on the terms the Trustee had offered TSF in order to settle as excessive. Judge Hoyt in that hearing also ominously said that when he retired in August he was going to go on recall status to keep this case, saying "you're going to love this." He added: "I'm going to keep this case. I'm going to finish this case."

On June 21, 2006, Hayes filed the Fee Application (#1858). On June 29, 2006, TSF objected to the Hayes' Fee Application (#1874). Also on June 29, 2006, TSF filed its Motion for Recusal (#1873). The grounds on which for TSF objected to Hayes' Fee Application included that "the files of this case reflect that the applicant has an actual conflict of interest in

representing at least one creditor the interests of which are adverse to the estate," and also that "during the time applicant has represented the Trustee, applicant has also represented interests adverse to the estate." TSF prayed for an order disallowing Hayes' Fee Application in its entirety.

On September 18, 2006, Hayes filed a Response to Objection To Application For Compensation And/Or Reimbursement of Attorneys Fees (#1931). In his Response, Hayes, for the first time, disclosed that when requested by Lovald to serve as his attorney, Hayes advised Lovald that he then represented one of the unsecured creditors, Clapper, and that at that time Lovald requested Hayes to "obtain a waiver of the conflict of interest from Clapper Corporation and was advised that the Trustee waived any conflict of interest in that regard." Hayes' Response also indicated that at the time when Hayes was contacted by Lovald, Hayes did not recall that early in the Chapter 11 proceedings he had represented an equipment lessor in connection with a default on an equipment lease by TSE. According to Hayes, the last activity by Hayes or his firm on that matter was concluded on January 27, 2004.

In the October 16, 2004, hearing on Hayes' Fee Application, Hayes testified that he represented Clapper at the time he became attorney for the Trustee in August 2004 (Tr. 10/16/06 hearing at 7:6-9); and his responsibility was to represent Clapper with respect to showing a proper filing of their proof of

claim and then monitoring the Chapter 11 proceedings (Tr. 10/16/06 hearing at 8:6-9). Clapper's proof of claim that was on file when Hayes was appointed was not in the amount of $178,500 but was in the amount of $195,929.43 (Claim No. 89). Schedule F showed that Clapper's claim was in the disputed amount of $178,500 (#22).

On January 6, 2006, Lovald, as Trustee, objected to the amended claim of Clapper in the amount of $95,630.29 and the dispute is ongoing (##1949, 1951; TSF-35 and 36).

Hayes also testified, however, as Hayes' Response stated, that before his appointment as attorney for Lovald had been approved, Hayes had obtained a waiver of any conflict of interest from both Clapper and Trustee (Tr. 10/16/06 hearing at 9:1-13; 9:25-10:13). He gave no testimony concerning TSE's claim in Schedule F that the Clapper claim was disputed or concerning the amendment by Clapper of its claim reducing it from $195,929.43 (POC No. 89) to $95,630.29 (POC No. 311), or to the Trustee's ongoing objections to reduce Clapper's claim more (##1949, 1951; TSF 35 and 36).

Yet, Hayes testified that before the Trustee objected to the Clapper claim, Hayes did nothing to investigate and inform himself as to whether there was in fact an actual conflict of interest; he claims that only after the Trustee objected to the Clapper claim did he understand that there was a dispute about the claim. (*Id.* at 10:21-11:1).

He further testified that to his knowledge at the time "there was no direct conflict between the Trustee and the creditor," and when asked whether he was able to say, he said, he can't testify beyond his knowledge. He claimed that he only learned there is dispute over the amount of the Clapper claim at the present time (Tr. 10/16/06 hearing at 11:20-12:1).

Still, after Lovald objected to the Clapper claim on January 6, 2006, Hayes knew of the conflict and was representing Clapper against Lovald in connection with Clapper's claim. At least as of June 5, 2006, Hayes was representing Clapper in connection with Lovald's Objection to Clapper's claim including exchanging documents and taking depositions (#1949; TSF-35). Between June 5, 2006, after depositions were taken, but before September 28, 2006, Hayes on June 21, 2006, filed Hayes Fee Application (#1858), TSF objected to Hayes Fee Application (#1874), and Lovald, who had been acting pro se or as his own attorney in objecting to Clapper's claim (#1662), engaged outside counsel to represent him against Clapper (#1949; TSF-35). So only after TSF objected to Hayes Fee Application did he face up to the actual conflict of interest between Lovald and Clapper.

The only compliance with Fed.R.Bankr.P. 214 that Hayes filed when appointed was the verification on Hayes' Fee Application (Tr. 10/16/06 hearing at 12:15-17). He conceded that he, as applicant, had the primary responsibility to know whether there was a conflict and to raise the issue (*Id.* at 13:5-8). Eventually, in his testimony, he testified that he did not

know whether there was an actual conflict or not when he was appointed but said, to the best of his knowledge, there was not (*Id.* at 15:5-12).

In the Motion for Recusal, TSF recited in summary that in the Chapter 7 case of TSE, there were major disputes between the Trustee, TSF, Murphy Brothers, and FDNB, that there was a major dispute over whether Lovald properly performed his fiduciary duties owed to TSF and over the amount of compensation to which Lovald may be entitled, and there were also other disputes between the Trustee and TSF over the allowance of other claims – including by its language the Hayes' Fee Application. In addition, TSF alleged that it held an equity security in TSE and as the holder of equity security in TSE, TSF is entitled to bring the Motion for Recusal. The grounds for recusal or disqualification of Judge Hoyt alleged in TSF's Motion for Recusal were, in summary, appearance of bias, actual bias against TSF, deep seated dislike and distrust and antagonism toward TSF and its members, including Hoich, Jandrain, Randy Kramer, and possibly Strasheim. The pattern of Judge Hoyt's rulings and statements against TSF, possible bias for NCC in litigation against TSF, and Judge Hoyt's involvement in aborted settlement efforts were alleged. The prayer of TSF was that Judge Hoyt recuse himself or be disqualified in all litigation of every kind and nature in the Chapter 7 case of TSE in which TSF either is a party or has an interest, including all contested matters and adversary proceedings.

Judge Hoyt, instead of ordering a hearing on the Motion for Recusal, *sua sponte* entered an "Order Setting Deadline for Joinders and Responses Re: Tri-State Financial's Motion for Recusal" (#1880) inviting "Any joinder in or response to "TSF's Motion For Recusal, and fixing August 20, 2006, as the deadline for any such joinder or response.

FDNB, with whom TSF has ongoing litigation, opposed TSF's Motion for Recusal (#1892), as did Lovald (#1893), and NCC (#1894). Randy Kramer, a member of TSF and owner of Western Biomass Energy, LLC (#1489) filed a Joinder in the Motion for Recusal as did TSF and as did James Jandrain, a member of TSF, and as did ICM (##1891, 1895, and 1896).[18] Lovald's objection was filed on August 20, 2006, included a lengthy affidavit eventually quoted at length by Judge Hoyt in his Decision (#1917) denying TSF's Motion for Recusal. On July 26, 2006, TSF filed a Motion for Leave to take the Deposition of Lovald in connection with the Motion for Recusal (#1904) and on the next day, July 27, 2004, Judge Hoyt entered an order transferring the case to Judge Kressel (#1905) who denied the motion (#1906). After TSF filed a Motion to Reconsider, Set Aside, Alter, or

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[18] Jandrain's and Kramer's claims were each heard and denied by Judge Hoyt on the same days as their hearings. FDNB opposed TSF's Motion for Recusal. Their claim was decided more than 100 days after their hearing. The theory under which they filed was denied, but the judge, on his own volition, allowed the claim based on a theory not even raised by FDNB.

Amend (former #1925) those orders denying TSF the right to take Lovald's deposition (#1911), Judge Hoyt entered a lengthy Decision and Order denying the Motion for Recusal (##1917, 1918), Judge Kressel on September 7, 2006, entered an order denying TSF's Motion to Reconsider, Set Aside, Alter, or Amend the change his previous order and let the deposition of Lovald be taken. TSF filed then filed a Motion to Reconsider, Alter, and Amend the Order denying TSF's Motion for Recusal as moot and was on its merits (#1921), which Judge Hoyt ordered struck the next day because not signed by local counsel as well as Omaha counsel (#1926). The Motion of TSF was physically removed from the Court's records of TSE's case (#1926).

On October 16, 2006, a hearing was held on the Hayes' Fee Application and the judge ruled from the bench that it should be granted. (Tr. 10/16/06 Hearing at 17:20-22). Later, on October 19, 2006, Judge Hoyt entered an order granting Hayes Fee Application (#1985). That order erroneously provides that TSF stipulated to the benefit to the estate or the necessity of the fees but correctly recited that applicant stipulated that the objection was whether or not Hayes had an actual conflict of interest as stated in the objection.

(F) ARGUMENT:

I. BY DENYING TSF DISCOVERY, AN EVIDENTIARY HEARING, AND THE OPPORTUNITY TO MAKE A FULL AND COMPLETE RECORD ON ITS RECUSAL MOTION, THE BANKRUPTCY COURT DENIED TSF DUE PROCESS, ABUSED ITS DISCRETION, OR BOTH.

When TSF filed its Motion for Recusal, instead of scheduling a hearing, on July 6, 2006, Judge Hoyt *sua sponte* entered an "Order Setting Deadline For Joinders and Responses Re: Tri-State Financial's "Motion for Recusal," fixing July 20, 2006, as the last day for filing such joinders and responses (Fil. #1880) ("Deadline Order").

As stated in the Deadline Order, Judge Hoyt took TSF's Motion For Recusal under advisement on July 20, 2006; also on July 20, 2006, Lovald filed Chapter 7 Trustee's Objection to Motion for Recusal of Tri-State Financial, LLC (Fil. #1893).

On July 26, 2006, three business days after July 20, 2006, TSF filed TSF's Motion For Leave To Take Deposition In Connection With Motion For Recusal (Fil. #1904) ("Motion For Leave"). Judge Hoyt *sua sponte* entered an Order Transferring Case To The Honorable Robert Kressel For Purpose of Ruling on Motion For Leave To Take Deposition In Connection With Motion For Recusal (#1905). On the same day, Judge Kressel entered an Order Denying Motion for Leave to Take Deposition (#1906) ("Denying Order").

On August 3, 2006, TSF filed a Motion to Reconsider, Set Aside, Alter and/or Amend Orders, asking as relief, among other things, that TSF be granted a hearing, and that TSF be allowed to engage in discovery and make a complete record (former #1925). The errors of law were supported by citation of authority. On September 7, 2006, Judge Kressel denied TSF's Motion to Reconsider, Set Aside, Alter, and/or Amend, saying that he saw "nothing in the motion which would leave me to revisit my order and in any case . . . the motion is now moot because Judge Hoyt has ruled on the merits of the underlying recusal motion."

All orders associated with the denial to TSF of any right of discovery on its Motion for Recusal, an evidentiary hearing, and the right to make a full and complete record are manifest errors of law. As was pointed out in TSF's August 3, 2006, Motion, as follows: It was erroneous to withhold any notice to TSF and deny TSF any opportunity to be heard after reasonable notice on the issues whether Judge Hoyt was authorized to enter the Transfer Order, whether Judge Kressel was authorized to enter the Denying Order, and whether the merits of TSF's Motion For Leave should be granted; this manifest error of law was exacerbated by nondisclosure to TSF of what papers were provided to Judge Kressel who, on information and belief, was in Minneapolis, Minnesota, and never came to South Dakota.

Further, it was erroneous to decide (i) that a factor relating to whether TSF was entitled to discovery on the Motion For Recusal was whether the

preceding commenced by the Motion For Recusal was or was not a contested matter and (ii) even if the Motion for Recusal commenced a contested matter, TSF was not entitled to discovery. Fed.R.Bankr.P. 4004 and 28 U.S.C. §455 both provide that disqualification of a bankruptcy judge is governed by 28 U.S.C. §455. Section 455 by its terms is applicable to "any justice, judge or magistrate judge of the United States." The procedure and whether discovery is available for motions to recuse non-bankruptcy justices, judges, and magistrates (that do not deal with "contested matters") is logically and necessarily the same as the procedure and whether discovery is available for bankruptcy judges (that do deal with "contested matters"). In a leading case, and probably the first to decide the issue, the court in *Cheeves v. Southern Clays, Inc.*, 797 F. Supp. 1570, 1580 (M.D. Ga. 1992), *aff'd without opinion*, 39 F.3d 326 (11th Cir. 1994), *cert. denied* 515 U.S. 1102 (1995) held that the discovery mechanisms under the federal rules of civil procedures are available to a party filing a motion for recusal under §455(a). In addition, *see In re Kensington Int'l Ltd.*, 368 F.3d 289 (3d Cir. 2004), discussed below. It was also erroneous to hold that there was a per se rule that TSF is not entitled to engage in discovery. Among the authority cited by TSF in TSF's Motion For Recusal is *Moran v. Clarke*, 296 F.3d 638 (8th Circuit 2002) (*en banc*). That case underscores that the recusal issue under 28 U.S.C. §455 (a) requires consideration of "all of the relevant facts." In a later opinion, the Court of Appeals repeated the need for "all the relevant facts." *Moran v.*

Clarke, 309 F.3d 516 (8th Cir. 2002) (*en banc*). *In re Kensington Int'l, Ltd.*, 353 F.3d 211 (3d Cir. 2003) makes clear that consideration of "all of the relevant facts" implicates the right to discovery. In *In re Kensington, supra,* the district judge who was presiding over a Chapter 11 case had *sua sponte* stayed discovery on the creditor's motions for recusal. The Third Circuit Court of Appeals held that the record was inadequate and incomplete, and that the district judge's stay of discovery prevented the parties from developing an adequate and complete record on the primary inquiry of whether, as provided under §455(a) "a reasonable person *knowing all of the circumstances* . . . would harbor doubts as to the judge's inquiry" (italics in original). The Court of Appeals in part stated:

> "First and foremost, we are concerned that the existing record is inadequate and incomplete . . . Judge Wilor[illegible] stay of discovery order prevented the parties from developing evidence of the circumstances which they allege give rise to the recusal motions. Hence, a remand allowing for discovery is necessary because the primary inquiry to which we must respond pursuant to 28 U.S.C. § 455(a) is "whether a reasonable person *knowing all the circumstances* would harbor doubts concerning the judge's impartiality" – an inquiry which necessarily requires that *we* know all the circumstances. . . . Accordingly, we require in order to discharge our judicial

> function that the evidentiary record in this case be developed. (Citation omitted).

353 F.3d at 323.

Had TSF been given reasonable notice and an opportunity to be heard, TSF would have had the opportunity to establish that: on July 5, 2006, counsel for TSF inquired by email to Kay Cee Hodson, Judge Hoyt's law clerk, whether Judge Hoyt *sua sponte* would schedule a hearing on TSF's Motion for Recusal; Ms. Hodson replied that "Judge Hoyt has advised me that no hearing will be held." (no Fil. #); the advice of TSF's attorney was that the 12/12/03 Decision and Order did not prevent Retrofitting the Ethanol Plant if not conditioned on super priorities, priming liens or treatment of FDNB; that the Retrofitting was not orchestrated by TSF and was not for the purpose of increasing the nameplate capacity of the Ethanol Plant from 14 MGY to 20 MGY; after the December 12, 2003, Decision and the December 12, 2003, Order, on advice of counsel, court approval was obtained for cash collateral of FDNB but not for loans by TSF which had no collateral; TSE timely reported all loans from TSF to the United States Trustee; much of the increase in capacity of the Ethanol Plant was done for reasons of prudent engineering and construction, cost of effectiveness and profitability; contrary to Lovald's affidavit and performance, the argument that there may be a return on equity is not reckless and misleading and allowed claims can be reduced sufficiently for a return on equity; initial drafts from NCC of the recited settlement between

TSE, TSF, and NCC provided they be attached to and confirmed with TSE's Plan; contrary to Judge Hoyt's statement on July 28, 2004, before the Retrofitting, the Ethanol Plant was never able to operate as intended; Judge Hoyt on July 27, 2004, to attempted to influence TSF to pay $2.5 million; and several other inaccuracies in Lovald's affidavit on which Hoyt relied; and other relevant facts.

The denial of discovery and an evidentiary hearing and the right to make a full record not only violated the due process rights of TSF and was an abuse of the court's discretion, it was accomplished by interlocutory orders based on erroneous understandings of the law.

II. EVEN ON THE RECORD AVAILABLE WITHOUT A HEARING, JUDGE HOYT ABUSED HIS DISCRETION IN NOT RECUSING HIMSELF.

TSF's Motion for Recusal is brought under 28 U.S.C. §455(a), relating to appearance of bias, the doctrine enunciated in *United States v. Pfizer, Inc.*, 560 F.2d 319 (8th Cir. 1977), dealing with a judge being too involved in settlement; 28 U.S.C. §455(b) relating to actual bias; and the Due Process Clauses of the United States Constitution.

It is provided in 28 U.S.C. §455(a) that a judge "shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned," *United States v. Pfizer Inc.*, 560 F.2d 319, 322-23 (8th

Cir. 1977) holds that a judge sitting as a trier of fact who has played an active and aggressive role in settlement and expressed strong opinions on the legal and factual issues of the cases creates an impression of bias; and, if the judge then assumes a fact finding function the judge may erode the right of a litigant to obtain a fair trial in fact as well as in appearance. *See also Alexander v. Primerica Holdings, Inc.*, 10 F.3d 155, 163, 166 (3rd Cir. 1993).

The disqualification in §455(a) is designed to promote public confidence in the integrity of the judicial process by replacing the subjective standard that was in the statute before 1970 with an objective test. *Liteky v. United States*, 510 U.S. 540, 548 (1994); *Moran v. Clarke*, 296 F.3d 638, 648 (8th Cir. 2002) (*en banc*). "By enacting section 455(a), Congress sought to eradicate not only actual, but also by the appearance of impropriety in the federal judiciary." *Moran v. Clarke*, 296 F.3d 638, 648 (8th Cir. 2002) (*en banc*). Under §455(a), actual bias is irrelevant. *Moran v. Clarke*, 296 F.3d 638, 648 (8th Cir. 2002) (*en banc*). The Eighth Circuit Court of Appeals has recast the issue under §455(a) to be "[w]hether the judge's impartiality might reasonably be questioned by the average person on the street who knows all of the relevant facts." *In re Kansas Public Employees Retirement System,* 85 F.3d 1353, 1358 (8th Cir. 1996). The inquiry under §455(a) about a judge's impartiality, including as it does "all the relevant facts", therefore, warrants consideration of Judge Hoyt's course or

pattern of rulings and his course of conduct. *Moran v. Clarke*, 296 F.3d 638, 649 (8th Cir. 2002) (*en banc*).

The doctrine enunciated in *United States v. Pfizer, Inc.*, mandates that the judge avoid even recommending an actual settlement amount before or during trial because "a fundamental principle of justice" is that "[i]t is important that a litigant not only receive justice, but that he believe he has received justice." 560 F.2d at 323.

"[w]here the question is close, the judge must recuse himself". *Union Planters Bank v. L & J Development Company, Inc.*, 115 F.3d 378, 383 (6th Cir. 1997).

In the Eighth Circuit a recusal order is interlocutory. *United States v. Brakke*, 813 F.2d 912, 913 (8th Cir. 1987); *Liddell v. Board of Education,* 677 F.2d 626, 643 (8th Cir. 1982); *Scarrella v. Midwest Fed. Sav. & Loan*, 536 F.2d 1207, 1210 (8th Cir. 1976); *Moix-McNutt v. Coop,* 215 B.R. 405, 407 (8th Cir. BAP 1997).

The grounds for recusal or disqualification under §455(a) cannot be waived until there has been a full disclosure on the record of the basis for disqualification; the grounds for disqualification under §455(b) cannot be waived. §455(e).

The facts here establish that Judge Hoyt gives every appearance of not being impartial with respect to TSF. He makes clearly erroneous findings of fact against but not for TSF. For example, his statement

about TSF's Plan in the July 28 hearing about the way TSF's Plan dealt with holders of equity security simply misstates the plan that was then on file. For another example, his statement as to disclosure that Retrofitting was continuing after his 12/12 ruling and 12/12 order is simply totally erroneous. He doesn't believe not only witnesses of TSF but witnesses that support the positions taken by TSF.

The facts also establish that Judge Hoyt often does not give TSF a reasonable opportunity to prepare for the trial; he treats attorneys for TSF different from the way he treats attorneys for the Trustee; he treats members of TSF that have claims different from members of the South Dakota bar; and he talks to reporters and pokes fun at members of TSF and possibly their attorney.

Judge Hoyt has a closed mind and does not allow for any possibility that, contrary to his expressed views, the evidence, if disputes to which TSF is a party were to go to trial, any of the following could possibly be the facts.

A. Since the Retrofitting of the Ethanol Plant was accomplished without any contract between TSE and ICM, without any management contract between TSE and United BioEnergy, without any super priority or other liens on TSE's assets, and without many of the attributes of a Chapter 11 plan included in the 09/25/04 Stipulation and Agreement, the Retrofitting was not an abuse of the bankruptcy process; and it was

reasonable for the parties to follow the advice of their former counsel. The decisions were all made to preserve the assets of the business and continue in the business of producing ethanol.

B. There was no nefarious scheme orchestrated by TSF or anyone to increase control of TSF.

C. The increase of the nameplate capacity of the Ethanol Plant from 14 MGY to 20 MGY was done for reasons of prudent engineering, cost effectiveness and profitability and was not orchestrated by TSF or any of its members. Much of the increase in capacity was the direct result of efficient operation and repair or replacement of what already existed, not expansion of the facility.

D. The loans that TSF offered to make and made were offered and made for the legitimate reasons that there was no other source of credit and not as part of any nefarious scheme.

E. The Retrofitting of TSE's Ethanol Plant was done to preserve the going concern value of TSE's Ethanol Plant.

F. A judge other than Judge Hoyt should preside over and resolve any claims that TSF violated Judge Hoyt's order; and another judge should also preside over and decide any and all contested matters and adversary proceedings to which TSF is a party or in which TSF should have an interest.

G. The appearance that Judge Hoyt might not be impartial toward TSF is pervasive in South Dakota and the other judge referred to in paragraph F should be a bankruptcy judge from another state such as Iowa.

Judge Hoyt punishes TSF and those associated with TSF for what he perceives to be misconduct. The punishment is unfair. The punishment is meted out in ways that the law does not provide. It would be one thing if Judge Hoyt had, after a hearing and notice, punished those involved with the Retrofitting on grounds for contempt of court – which they were not guilty of – or for violation of the automatic stay, or because creditors by appointing a trustee, brought a proceeding. But Judge Hoyt instead punishes those who have participated in the Retrofitting by denying their claims, and by treating them as not deserving of equity.

The fact is that the reason the creditors and other interested parties have such a recovery in this case is because of the Retrofitting. There is no legitimate reason to hold otherwise. Moreover, the Court has been aggressively involved in settlement. The anchors of his mind are the numbers in the settlement discussions.

The grounds for recusal under §455(a) are not waivable until after full disclosure and Judge Hoyt has not made such disclosure. The grounds under §455(b) are not waivable. §455(e). *In re Kansas Public*

Employees Retirement System, 85 F.3d 1353, 1359 (8th Cir. 1996).

It is respectfully submitted that the decision of Judge Hoyt (#1917) denying TSF's Motion for Recusal is itself substantial evidence of Judge Hoyt's bias against TSF. As Judge Hoyt himself points out, *Liteky v. United States*, 510 U.S. 540, 551 (1994) states that a judge's "favorable or unfavorable predisposition can . . . deserve to be characterized as 'bias; or 'prejudice' because, even though it springs from the facts adduced or the events occurring at trial, *it is so extreme* as to display clear inability to render fair judgment." Judge Hoyt's Decision (#1917) on TSF's Motion for Recusal (#1873) reinforces the bases for recusal alleged in TSF's motion and illustrated by the facts summarized above, and as Judge Hoyt's decision itself demonstrates, the bias is so extreme as to display clear inability to render fair judgment.

The reasonable inference from Judge Hoyt's comments on May 4, 2004, that he was retiring but going on recall is that he intends to assure that TSF will not overcome his views about whether the petition was filed by TSE in good faith, whether TSF deliberately disregarded his authority and whether TSE schemed to get increased equity in TSE – in other words that TSF will not receive a fair trial before him. *Liteky v. United States*, 510 U.S. 540, 558 (1994).

The length of Judge Hoyt's Decision (#1917) and the maximum length of this brief does not permit

TSF to offer comments on Judge Hoyt's Decision point-by-point. But, to begin with, some of its inaccuracies are listed in TSF's Motion to Reconsider, Alter, and/or Amend Decision (former #1925) which Judge Hoyt struck and caused to be physically removed from the file of TSE (#1926). The inaccuracies all work against TSF; none has been found that favor TSF.

There are mis-descriptions or half descriptions in Judge Hoyt's Decision that are slanted against TSF. One instance is Judge Hoyt's quotation of the recitation of an agreement in court on June 21, 2004. While quoting language, Judge Hoyt omits the language that a written agreement was to be prepared and none was agreed upon. Judge Hoyt later held that there was no meeting of minds (#933).

Another instance is Judge Hoyt's use of the term "re-engineering". Judge Hoyt knows that TSF has objected to the Trustee's prepared $2 million settlement with NCC; an issue of significance is whether the plant's failure to operate after it was completed or nearly completed in 2002 was caused by faulty and defective engineering, by faulty and defective construction, or by both; and TSF maintains that the failure of the plant to operate was caused by faulty construction as well as by faulty engineering. Instead of picking a neutral term such as Retrofitting, Judge Hoyt uses the phrase "re-engineering" to include both, thereby favoring the Trustee and disfavoring TSF. (#1917). Judge Hoyt transmogrifies TSE's 9/25/03 motion and the 9/25/06 Stipulation between

TSE, TSF, and FDNB supporting that motion, as a motion for solely re-engineering which it was not. (#1917 at page 7, note 3). Judge Hoyt then inaccurately characterizes the testimony of VanderGriend on July 28, 2006, as to the work ICM had been doing up to that date without a contract, as work "to increase its production capacity to 20 million gallons per year." (*Id.* at 30). He adds descriptions apparently designed to mischaracterize VanderGriend as not knowing facts on which he testified by reference to VanderGriend's testimony on July 28, 2004, that he thought the claims against TSE totaled $5 million. (*Id.* at 31). The Court questioned VanderGriend on the subject and knows or should know that his field of knowledge was not the debt against the Ethanol Plant but the Retrofitting to make it work. Moreover, Judge Hoyt neglects to mention that when Jandrain was called to the stand on July 28, 2004, he testified from schedules of debt that Jandrain had proposed, the schedules were accurate, and there was no doubt as to the parameters of the debt of TSE after Jandrain's testimony. (*Id.* at 32).

In his Decision, Judge Hoyt inaccurately had John Hoich at the June 21, 2004, hearing, from which Judge Hoyt quotes much testimony, when Hoich was neither there nor had a representative there. (#1917 at 25-26). And contrary to Judge Hoyt's opinion (#1917 at 23), June 8, 2006, is not the first statement in the record that TSF had continued retrofitting the plant after the Court entered its 12/12/03 decision; and in fact TSE had made full disclosure of its

re-engineering and reconstruction in disclosure statements filed December 31, 2003, 19 days after Judge Hoyt's December 12, 2003, opinion, and again on February 17, 2004.

Judge Hoyt, in his Decision, confirms his bias, saying TSF "had now backed away twice from settlements announced on the record" and that "counsel for TSF again took exception." It is difficult to understand why the court makes these statements but refuses to look at drafts and letters exchanged and evidence that the parties could not reach written agreements.

In the February 9, 2006, hearing, Judge Hoyt characterizes proceedings as one in which Strasheim "suddenly announced" that TSF did not oppose enforcement of [the] core agreements even though in TSF's written opposition to NCC's motion filed on December 14, 2005, TSF had plainly stated that TSF did not oppose enforcement of the core agreements according to their terms (#1637 at ¶23); he erroneously said that "Strasheim argued at length his personal written understanding of the July 26, 2005, mediation results . . . " (*Id.* at 60) when Strasheim was actually trying to identify the core agreements comprising the operative contractual language. Strasheim offered in evidence only quotes from the mediation transcript to separate operative contractual language from other language in the core agreements. Judge Hoyt does not deny the sworn statements contained in the Affidavit of Grace "Mimi" Larsen. These comments reflect statements of Judge

Hoyt in an interview, not a trial or judicial proceeding.

It is misleading for Judge Hoyt to state that there are no matters pending before the court in which the debtor's failure to get court authority for the re-engineering project is at issue, no such issues are expected to arise in the future, and TSF's claim was already resolved by order (#1917 at 84). TSF not only holds a subordinated claim, but also holds equity security in the debtor (#1409). The recovery by TSF on its claim, $1,190,000 of which is subordinated to other claims, can be diminished by the court allowing other unmeritorious claims. These include claims of Murphy Brothers in which there is nearly $800,000 at stake (#1462), the claim of NCC, which the Trustee wants to settle for $2 million and which TSF claims should be tried or settled for substantially less than $2 million, and the claims for attorneys and other professional fees. In all of these instances, Judge Hoyt knows that by allowing other claims, he diminishes either the recovery by TSF on its allowed subordinated claim, and/or recovery by TSF on its over 40% equity (#1409).

Recently, Judge Hoyt has allowed a claim for FDNB in the amount of $173,000 on a basis that had not even been argued, after Judge Hoyt had sent signals that the claim was not going to be allowed at all (##2023 & 2002). TSF has appealed from that order. That illustrates the injury that TSF can suffer if other cases in this case are decided by Judge Hoyt.

The six bases alleged in TSF's Motion for Recusal are established; Judge Hoyt has apparent bias toward TSF and actual bias toward TSF. Trial of disputes involving or affecting TSF violates due process. The decision of Judge Hoyt denying TSF's Motion for Recusal reinforces that TSF cannot get a fair trial before Judge Hoyt.

Since Judge Hoyt was required to recuse himself, any orders following his denial of the Motion for Recusal should be vacated. *Republic of Panama v. The American Tobacco Co., Inc.*, 217 F.3d 343, 347 (5th Cir. 2000).

III. AS HIS GENERAL ATTORNEY, AN ATTORNEY MAY NOT BE EMPLOYED BY A CHAPTER 7 TRUSTEE IF THE ATTORNEY HAS AN ACTUAL CONFLICT OF INTEREST.

The qualifications prerequisite to employment of professionals are set forth in 11 U.S.C. §327. Section 327(a) provides:

> (a) Except as otherwise provided in this section, the trustee, with the court's approval, may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties under this title.

This section creates a two-part requirement for representation of counsel: counsel must "not hold or represent an interest adverse to the estate" and must be a "disinterested person". The Bankruptcy Code does not contain a definition of "interest adverse to the estate" but does define interested person in 11 U.S.C. §101(14).

Section 327(a) provisions must be read with Section 327(c) which insofar as relevant provides that in a Chapter 7 case, an attorney is not disqualified for employment under §327(a) "*solely* because of such person's employment by or representation of a creditor, unless there is objection by another creditor or the United States Trustee, in which case the court shall disapprove such employment if there is an actual conflict of interest." (Emphasis added).

Section 328(c) provides that the court may disallow compensation for attorneys employed under 327 "if at any time during such professional person's employment under §327 . . . such professional person is not a disinterested person, or represents or holds an interest adverse to the estate with respect to the matter on which the professional person is employed." (Emphasis added).

The provisions of §327 are supplemented by Federal Rule of Bankruptcy Procedure 2014, which creates a disclosure requirement to enforce the standards of 327(a).

When appointed, Hayes had the affirmative duty to make a full, candid and complete disclosure of not only his representation of Clapper but also that Clapper claim was disputed and dual representation of Clapper and Lovald entailed Hayes representing an interest adverse to and in conflict with the interest of the Chapter 7 Estate. *In re Coastal Equities, Inc.*, 39 B.R. 304, 308 (Bankr. S.D. Cal. 1984). Hayes' subjective intent or state of mind is irrelevant. *In re Granite Sheet Metal Works, Inc.*, 159 B.R. 840, 845 (Bankr. S.D. Ill. 1993).

Hayes' mere conclusive statement in the verification was insufficient because it was incomplete. *In re Azevedo*, 92 B.R. 910, 911 (Bankr. E.D. Cal. 1988). Section 327 must be strictly construed in order to maintain the integrity of the bankruptcy process. *In re American Energy Trading, Inc.*, 291 B.R. 154, 157 (Bankr. S.D. Mo. 2003). Negligent omissions do not vitiate the duty to disclose. *In re Mich General Corp.*, 78 B.R. 479, 482 (Bankr. N.D. Tex. 1987).

IV. A CHAPTER 7 TRUSTEE HAS NO POWER TO WAIVE CONFLICTS.

Here, the Trustee and Hayes apparently believe they can agree to waive the conflict in order that the Trustee might employ Hayes. This simply is not so. *In re American Energy Trading, Inc.*, 291 B.R. 154, 157, 158 (Bankr. W.D. Mo. 2003); *In re Perry,* 194 B.R. 875, 879, 880 (E.D. Cal. 1996).

V. SECTION 327(a) AND §327(c) IMPOSE A PER SE DISQUALIFICATION AS TRUSTEE'S COUNSEL OF ANY ATTORNEY WHO HAS AN ACTUAL CONFLICT OF INTEREST.

In re Pillowtex, Inc., 304 F.3d 246 (3d Cir. 2002), cited by the Missouri Bankruptcy Court in *American Energy Trading, supra*, is authoritative and clear. There, the court stated that its earlier holdings were that:

> (1) Section 327(a), as well as §327(c), imposes a per se disqualification as trustee's counsel of any attorney who has an *actual conflict of interest*; (2) the district court may within its discretion-pursuant to §327(a) and consistent with §327(c) – disqualify an attorney who has a *potential conflict of interest* and (3) the district court may not qualify an attorney on the *appearance of conflict* alone (emphasis of italics in original; emphasis of underlining added).
>
> . . .
>
> In *In re First Jersey Securities, Inc.*, 180 F.3d 504 (3d Cir.1999), the U.S. Trustee objected to retention of the counsel proposed by the debtor in possession on the ground that counsel had received a preferential payment, constituting an interest adverse to the estate. Notwithstanding that both the bankruptcy court and the district court had approved counsel's retention, this court reversed. We stated that "[w]here there is an actual conflict of interest . . . disqualification

> is mandatory." *Id.* at 509 (citing *In re Marvel Entertainment,* 140 F.3d at 476).

304 F.3d at 251-52.

The per se rule should be applied here for the reasons contained in the above cases; the Court should not reward playing fast and loose with the disclosure requirements; and the Court should disallow Hayes' Fee Application as provided in 11 U.S.C. §328(c) if not requiring him to disgorge fees already allowed and paid.

VI. THE BURDEN OF PROOF WAS ON HAYES.

The clearly erroneous finding of fact by Judge Hoyt that Hayes had no actual conflict of interest when employed by Lovald results solely from a misplaced burden of proof. The burden of proof at the hearing on Hayes' Fee Application was on Hayes to establish his right to fees. The burden was on Hayes to come forward and make a full, candid, and complete disclosure. *In re Roberts,* 75 B.R. 402, 411-12 (D. Utah 1987) (*en banc* aff'd. 46 B.R. 815, 839). This was a burden he could have met by simple inquiry, especially after Lovald objected to the Clapper claim. Having failed to meet his burden of proof, the court should have found that there was no actual conflict. Moreover, Hayes is bound by the judicial admission in his response that there was an actual conflict that was waived. *State Farm v. Worthington,* 405 F.2d 683, 686 (8th Cir. 1968). Hayes should have denied compensation. The order entered misstates the stipulation of TSF on the record.

Thus, where because there was no disclosure by Hayes of an actual conflict of interest existing at the time, Hayes' employment was void *ab inititio*, and his services are not entitled to compensation. *In re EWC, Inc.*, 138 B.R. 276 (Bankr. W.D. Okla. 1992).

CONCLUSION

The Order Approving Application for Compensation of Attorney Robert E. Hayes should be reversed.

Dated this 28th day of November, 2006

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